2001

HSBC Bank Canada

Annual Report and Accounts

The world's local bank

HSBC

CORPORATE PROFILE

HSBC Bank Canada, a subsidiary of HSBC Holdings plc, has more than 160 offices. With over 7,000 offices in 81 countries and territories and assets of US$696 billion at 31 December 2001, the HSBC Group is one of the world's largest banking and financial services organizations.

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Shareholder Information

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STOCK EXCHANGE LISTINGS

HSBC Bank Canada Class 1
Preferred Shares Series A
(TSE: HSB.PR.A)

HSBC Canada Asset Trust
Securities Series 2010 (HSBC HaTS)
(TSE: HBH.M)

TRANSFER AGENT AND REGISTRAR

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Shareholder Service Department
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SHAREHOLDER CONTACT

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Other shareholder inquiries may be directed to our Shareholder Relations Department by writing to:

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This document may contain forward-looking statements, including statements regarding the business and anticipated financial performance of the Bank. These statements are subject to a number of risks and uncertainties that may cause actual results to differ materially from those contemplated by the forward-looking statements. Some of the factors that could cause such differences include legislative or regulatory developments, competition, technological change, global capital market activity, changes in government monetary and economic policies, changes in prevailing interest rates, inflation levels and general economic conditions in geographic areas where the Bank operates.

The information contained in management's discussion and analysis is derived from the audited consolidated financial statements of the Bank. Effective for 1998, the Bank changed its fiscal year-end from October 31 to December 31 to be consistent with that of HSBC Holdings plc. As well as being presented on an actual basis, the information for the fourteen months ended December 31, 1998 included in the five year summary has been annualized for comparative purposes. The annualized amounts are unaudited and were calculated by multiplying the audited results for the fourteen months ended December 31, 1998 by 12/14ths. The data under Risk-based Capital Ratios, Financial Ratios and Other Financial Data in various tables are derived from financial information used to prepare the audited consolidated financial statements of the Bank.

Unless otherwise stated, all references to $ means Canadian Dollars.

Five Year Financial Summary

(in millions, except ratios)

	Year ended December 31, 2001	Year ended December 31, 2000	Year ended December 31, 1999	Fourteen months ended December 31, 1998 (annualized) (Unaudited)	Fourteen months ended December 31, 1998	Year ended October 31, 1997
Statement of Income Data						
Net interest income	**$ 754**	$ 666	$ 540	$ 519	$ 606	$ 493
Provision for credit losses	**92**	39	43	77	90	38
Net interest income after provision for credit losses	**662**	627	497	442	516	455
Other income	**419**	462	384	285	332	240
Net interest and other income	**1,081**	1,089	881	727	848	695
Non-interest expenses						
Salaries and employee benefits	**359**	385	339	266	310	230
Premises and equipment(1)	**115**	108	101	86	100	72
Other	**230**	249	197	183	214	172
Total non-interest expenses	**704**	742	637	535	624	474
Income before taxes	**377**	347	244	192	224	221
Provision for income taxes	**147**	155	79	36	42	83
Non-controlling interest in income of subsidiaries	**16**	8	–	–	–	–
Net income	**214**	184	165	156	182	138
Preferred share dividends	**8**	15	–	–	–	–
Net income attributable to common shares	**$ 206**	$ 169	$ 165	$ 156	$ 182	$ 138
Balance Sheet Highlights (at period end)						
Total assets	**$ 33,260**	$ 29,438	$ 25,051	$ 24,836	$ 24,836	$ 23,910
Total loans	**21,870**	19,753	17,130	17,459	17,459	16,454
Commercial loans	**11,575**	11,330	9,634	9,934	9,934	7,940
Residential mortgage loans	**8,377**	6,809	5,769	6,057	6,057	6,876
Total deposits	**26,707**	23,511	20,170	20,550	20,550	20,115
Personal deposits	**13,390**	12,116	10,858	10,213	10,213	9,922
Subordinated debentures	**447**	422	392	620	620	549
Shareholders' equity	**1,612**	1,406	1,252	817	817	671
Risk-based Capital Ratios (%) (at period end)						
Tier 1 Capital	**8.6**	8.6	7.9	5.4	5.4	4.7
Total Capital	**11.3**	11.5	10.9	10.0	10.0	8.9
Financial Ratios (%) (at period end)						
Return on average common equity	**14.9**	15.3	18.4	21.0	21.0	20.2
Return on average total assets	**0.65**	0.60	0.63	0.63	0.63	0.61
Other income percentage(2)	**35.7**	41.0	41.6	35.4	35.4	32.7
Cost:income ratio(3)	**59.3**	65.2	68.8	66.5	66.5	64.7
Net non-performing loans as a percentage of loans and acceptances(4)	**(0.14)**	(0.51)	(0.55)	(0.67)	(0.67)	(0.39)
Liquidity ratio(5)	**27.4**	25.5	22.6	24.3	24.3	25.0
Funds Under Management (at period end)	**$ 10,559**	$ 10,198	$ 10,227	$ 7,332	$ 7,332	$ 5,022

(1) *Premises and equipment expenses, including amortization.*

(2) *Other income percentage is other income as a percentage of the total of net interest income and other income ("other income percentage").*

(3) *Cost:income ratio is total non-interest expenses as a percentage of the total of net interest income and other income, excluding amortization of goodwill and intangible assets ("cost:income ratio").*

(4) *Net of specific and general allowances for credit losses.*

(5) *Liquidity ratio is liquid assets as a percentage of total deposits (liquidity ratio).*

Message from the President and CEO

A strong team of employees, focused and working hard, coupled with an improved interest rate environment, helped us overcome a challenging economic environment and finish 2001 with very positive results. Our core businesses performed strongly, with improved profitability from all business lines.

During this time of uncertainty in the markets, we strived to be more effective at recognizing and meeting the needs of all clients and to provide the kind of counsel, support and advice they required. We were also very proud of the increasing recognition we received from independent market surveys, of the high quality of our customer service.

The world-changing events of September 11 have had a negative economic impact in Canada. The full impact on future economic conditions is not known although, to date, our business has held up well and the effects on our customers have not been significant. We are working closely with all clients during these continuing challenging times to understand their needs and to offer solutions drawn from our global connections and the financial strength of the HSBC Group.

We recently announced a much closer working relationship between HSBC Bank USA and HSBC Bank Canada. A comprehensive North American alignment initiative has been developed, in part, to provide seamless North American service propositions to our customers. Our goal is to be known as North America's premier cross-border bank, which ties in with the HSBC Group's new brand positioning as "The world's local bank."

Aligning our American and Canadian operations will allow management to better leverage the strengths and best practices of each bank. It will also enable us to increase economic profit in North America by improving HSBC's position in terms of brand awareness, cost efficiencies, revenue generation, distribution and risk management. At the same time we will be able to provide greater career satisfaction and development for more of our employees with opportunities that extend beyond domestic borders.

While prospects for 2002 are somewhat uncertain, the fact remains that we have entered the year with a very strong and positive momentum. Our excellent customer service and expertise as "The world's local bank" should continue to strengthen our relationships with our customers. If we maintain our momentum and enthusiasm and allow it to carry us forward throughout the year, we will build upon our achievements in 2001 and succeed again in 2002.

Martin J. G. Glynn
President and Chief Executive Officer

Management's Discussion and Analysis

For the year ended December 31, 2001

Overview

HSBC Bank Canada ("HSBC") is the largest full-service, internationally owned bank in Canada. It is the seventh largest bank overall, operating in every region in Canada, with total assets of $33.3 billion at December 31, 2001. As an indirectly held subsidiary of HSBC Holdings plc ("HSBC Holdings"), clients are provided with access to one of the largest banking and financial services organizations in the world. Through its worldwide network of more than 7,000 offices in 81 countries and territories, the HSBC Group provides a comprehensive range of financial services to clients worldwide and enjoys a leading market position in trade services and other products in many markets around the world.

Originally established in 1981 with our head office located in Vancouver, British Columbia, we have grown, mainly by acquiring new customers through our reputation for providing superior customer service, and through strategic acquisitions, to become a fully integrated financial services organization. With more than 160 offices across Canada and two offices in the north-western United States, we provide personal and commercial financial services, together with subsidiaries that offer full service brokerage, fund management, trust and advisory, investment banking and direct sale of home, auto and travel insurance. Online investment services for self-directed investors are provided through our strategic partner Merrill Lynch HSBC Canada Inc. ("Merrill Lynch HSBC"), a subsidiary of Merrill Lynch HSBC Ltd, the worldwide online investment and banking company.

The HSBC Group

Established in 1865, the HSBC Group is one of the largest banking and financial services organizations in the world, with a market capitalization of US$109 billion at December 31, 2001. At the end of 2001, the HSBC Group had total assets of US$696 billion, shareholders' equity of US$46 billion and total funds under management of US$284 billion. For the year ended December 31, 2001, the HSBC Group's consolidated operating profit was US$7.2 billion on revenues of US$25.9 billion. HSBC Holdings is strongly capitalized under UK standards (which are comparable to those in Canada) with a Tier 1 capital ratio of 9.0% and a total capital ratio of 13.0% at December 31, 2001. The ordinary shares of HSBC Holdings are listed on the London, Hong Kong and Paris stock exchanges. Its American Depositary Receipts are listed on the New York Stock Exchange. Headquartered in London, the HSBC Group operates through long-established businesses in Europe, the Asia-Pacific region, the Americas, the Middle East and Africa.

In 2002 HSBC will be launching an ambitious new worldwide branding campaign centered on its new positioning statement, "The world's local bank." The campaign's objective is to maintain and improve HSBC's position as one of the world's leading financial services brands. The campaign demonstrates the true relevance of HSBC's global and local market expertise. Consumers understand they need the advantages of a worldwide scale bank but they want to balance that strength with local market understanding and a high level of personal service. HSBC has the unique ability to harness genuinely local, on-the-ground expertise from all over the world to bring people better financial solutions. That is why HSBC is "The world's local bank."

The Business of HSBC Bank Canada

Strategy

Our objective is to be the leading international provider of financial services in Canada with a significant presence in identified key markets. In 2000, we introduced a five year strategic plan entitled "Managing for Value" designed to support the HSBC Group's key strategic initiatives. The strategy continues to be to expand and build on our strengths as a provider of financial services to small and midsize companies as well as personal financial services to individuals. The provision of commercial financial services, including trade finance, treasury and capital market products to large corporates continues to be a focus. To achieve this, we will utilize the international capabilities of the HSBC Group to provide our customers with excellent service in Canada. Our strategy has the following key operating components:

- **Leverage the worldwide strength and reach of the "HSBC" brand to expand customer base and geographic presence** – We believe the international strength and reach of the "HSBC" brand is our most significant competitive advantage. We intend to increase Canadian awareness of the HSBC Group's international capabilities to enhance our market share and realize economies of scale in Canada. While our strategy is focused principally on organic growth, it also allows for opportunistic acquisitions.
- **Deepen existing client relationships** – We are focused on increasing penetration of our customer base by better understanding and meeting clients' needs and ensuring they have ready access to the full range of our products and services and the global capabilities of the HSBC Group.
- **Re-engineering organizational processes and structures to optimize efficiency, while enhancing sales and advisory activities** – We will implement a variety of strategies which will promote operating efficiency by supporting an increased focus by our branch staff on sales and relationship management. This will mean redistributing resources to ensure they are deployed so as to maximize our sales potential.
- **Ensuring systems development, capacity and performance continue to address the changing and growing needs of HSBC and its clients** – We will take full advantage of our HSBC Group connections by leveraging the HSBC Group's technology investments as we build and enhance our systems.
- **Enhance multi-channel delivery systems** – We are focused on improving customer service by providing increased choice for delivering services through a variety of channels. While our branch network will remain a critical delivery channel, we plan to expand the market for telephone and PC based banking services such as Internet banking. We are also implementing a focused e-business strategy to enhance electronic delivery capabilities.
- **Attract, retain and motivate a high performance team of employees** – This policy has been critical to our success and the development of a strong sales and service culture throughout the organization.

Business Lines

We offer a wide range of products and services to targeted segments of the financial services market, through four major business segments, Personal Financial Services, Commercial Financial Services, Corporate and Institutional Banking and Treasury and Markets. The organization and structure of our operations focus on customer needs, and are uniquely integrated across service and product lines, subsidiaries, and strategic alliances and internationally through the HSBC Group's international network.

- **Personal Financial Services** provides our personal customers in Canada, and where appropriate worldwide, with excellent customer service and offers access to a comprehensive range of financial products and services through a variety of delivery channels.
- **Commercial Financial Services** provides a complete range of financial products and services to Canadian commercial clients. Commercial Financial Services are provided through our branch network and subsidiary offices in Canada as well as through other HSBC Group offices around the world.
- **Corporate and Institutional Banking** provides a large range of financial services to the HSBC Group's large multinational clients. The focus of Corporate and Institutional Banking is on entities that have a need for global value-added products including investment banking, structured lending and trade services.
- **Treasury and Markets** consists of three principal activities – client trading and facilitation, proprietary trading and balance sheet management. The HSBC Group's international treasury and capital markets capabilities are used to enhance the opportunities to serve our customers

During 2001, we realigned some of our operations and combined the Corporate and Institutional Banking ("CIB") business together with the Commercial and Institutional segments of our brokerage and asset management businesses to form a new business unit, "Wholesale Banking." For 2002, the results of this unit will be tracked separately and will replace CIB as one of our reported business lines.

Management's Discussion and Analysis (continued)

Review of Operations – 2001

2001 Highlights

- We expanded delivery of HSBC *Premier* in Canada (a global product, offering an exclusive suite of banking, credit and investment services and special privileges). We also launched Global Private Client Services in Vancouver and Montreal. We opened our new flagship branch in downtown Montreal, relocating various core bank and subsidiary offices into one customer-focused banking centre.
- We enhanced our sales management processes, resulting in significant residential mortgage growth and increased funds under management despite difficult market conditions. In 2001, HSBC Mutual Funds ranked as the third fastest growing family among the top 30 mutual fund companies in Canada ranked by size.
- We received a number of independent awards and were top ranked for our personal and commercial customer service, including being rated the highest amongst all Canadian financial institutions for overall quality of service.
- We celebrated our 20th anniversary in Canada with a major effort to increase brand recognition culminating in becoming a title sponsor of the "HSBC Power Smart Celebration of Light" international fireworks festival in Vancouver.
- We opened an additional call centre in central Canada to increase our direct banking capacity. This centre also handles Cantonese and Mandarin language service for HSBC Bank USA.
- We increased the client base of our Personal Internet Banking service by more than 400% and introduced Commercial Internet Banking in December 2001. We joined other HSBC Group members in providing customer access to "FX-All," a multi bank global foreign exchange trading portal.

Financial Results

- Net income attributable to common shares increased 21.9% to $206 million for the year ended December 31, 2001 compared to $169 million in 2000.
- Income before taxes and non-controlling interest in income of subsidiaries was $377 million for the year ended December 31, 2001, an increase of 8.6% over 2000.
- The cost:income ratio (excluding amortization of goodwill and intangible assets) improved to 59.3% in 2001 from 65.2% in 2000.
- Total assets of $33.3 billion at December 31, 2001 ($29.4 billion at December 31, 2000).
- Total capital ratio of 11.3% and tier 1 capital ratio of 8.6% at December 31, 2001 (11.5% and 8.6% respectively at December 31, 2000).
- Funds under management were $10.6 billion at December 31, 2001 compared to $10.2 billion at December 31, 2000.

Achievements for 2001

Some of our achievements in pursuing our strategy for 2001 included the following:

Leverage the worldwide strength and reach of the "HSBC" Brand to expand customer base and geographic presence. As part of the HSBC Group, we provide clients with access to the HSBC Group's worldwide strength, reach and brand, which is considered to be a significant competitive advantage. As an example, a Canadian HSBC ABM card can be used at 30,000 ABM machines in Canada and more than 600,000 worldwide, including any HSBC Group ABM machine wherever it is located.

In Canada, we continue to have success in marketing the HSBC *Premier* product to key customers. This is a global product that offers an excellent suite of banking, credit and investment services and special privileges to our customers.

In 2001, we celebrated the 20th anniversary of HSBC Bank Canada. Various receptions were held recognizing the importance of our customers in contributing to our success during the period. The importance of the community at large, as part of our success, was recognized when we became one of the title sponsors of the "HSBC Power Smart Celebration of Light" international fireworks festival in Vancouver, which was held in July and August and attended by more than 1.6 million people. We were also a 2001/2002 season sponsor for Roy Thomson Hall and Massey Hall in Toronto, providing exposure to the "HSBC" brand at many events throughout the period.

Deepen existing client relationships. During 2001, we received strong third party endorsement of our superior customer service. In the 2001 Customer Service Index produced by Market Facts of Canada, HSBC was rated the highest among all financial institutions in Canada for "overall quality of service"; 97.1% of users surveyed rated HSBC customer service as "good", "very good" or "excellent". In the December/January 2002 edition of "MoneySense" magazine, an industry periodical, HSBC Mutual Funds were ranked as the best bank-owned mutual fund family in Canada. Respondents to the Canadian Federation of Independent Business survey (Banking on Entrepreneurship, March 2001) ranked HSBC first among Canadian banks for "understanding my business."

McGill College Avenue, in downtown Montreal, is the location for our new flagship branch, which opened in June 2001. Our existing downtown locations, including one acquired with Republic National Bank of New York (Canada) in 2000, were combined into one customer-focused regional banking centre. This included relocating the subsidiary offices of HSBC Securities (Canada) Inc. and HSBC Asset Management (Canada) Limited, creating greater synergies for the benefit of our customers as well as for us.

Much progress has been made during 2001 to develop a national sales and relationship management process to ensure consistent service while maximizing business opportunities. In 2002 we will introduce "*Client*Connect," a system that will streamline front end processing, assisting our staff to serve customers more effectively.

Re-engineering organizational processes and structures to optimize efficiency, while enhancing sales and advisory activities. We continue to focus on re-engineering and improving processing efficiency. Managing service and delivery channels to more efficiently meet customer needs and expectations as they evolve over time continues to be a priority. We began the roll-out of a centralized call management program in mid-2001, which will be completed in 2002. Call management has improved customer service, as calls are handled by dedicated, highly trained staff, who are supported by modern systems and technology. Other operating efficiencies have allowed further reallocation of resources from administrative to sales functions and we are in the process of centralizing our home loan processing.

In Canada we will continue to work with HSBC Bank USA and the HSBC Group to take advantage of the HSBC Group's global back office processing capabilities. Our new direct banking telephone centre, which opened in Toronto in March 2001, provides a call centre for customers in Central and Eastern Canada as well as disaster recovery back-up for the Vancouver call centre. Our ability to support Cantonese and Mandarin speaking clients has enabled us to support similar customer enquiries for our affiliate HSBC Bank USA's call centres.

Ensuring systems development, capacity and performance continue to address the changing and growing needs of HSBC and its clients. We continue to update systems and technology to leverage economies of scale through the use of HSBC Group systems such as core and Internet banking platforms. Upgrades completed in 2001 included installation of updated core banking software, which provides us with a new base to further enhance customer service. Systems upgrades scheduled for 2002 are expected to further enhance our capabilities.

As part of its global initiatives, the HSBC Group's systems development facility in Burnaby, BC takes a leading role in the development of sophisticated banking, e-business and support systems for the HSBC Group worldwide. We are able to benefit from the early implementation of these systems to improve our operations and customer service capabilities.

Enhance multi-channel delivery systems. We plan to increase the use of technology to speed up decision making for customer credit applications by implementing in 2002, on a limited basis, systems for automated credit adjudication of personal loan applications. Systems for automated credit scoring as well as management tools are being developed to improve service in Commercial Financial Services. This improvement in efficiencies is also expected to benefit our cost:income ratio.

Our e-business strategy continues to develop. Registration for Personal Internet Banking has increased by more than 400% in 2001 and Commercial Internet Banking was introduced in December 2001. Further upgrades for both products are planned for 2002. Together with Merrill Lynch HSBC, we installed Internet enabled kiosks in our main offices as part of an overall strategy to showcase the Internet based service options of both HSBC and Merrill Lynch HSBC through our branch network.

Attracting, retaining and motivating a high performance team of employees and developing a consistent culture of excellence through sales and service. We continue to focus resources on high performing employees, increasing rewards for those who achieve superior performance benefiting the organization and shareholders. In 2001, our CEO announced the first recipients of the President's Awards. Winners participated in a select recognition program, including membership in the President's Council, which acts in an advisory capacity to the President and Chief Executive Officer.

Management's Discussion and Analysis (continued)

In 2001, we introduced a number of work-life balance policies, which have been well received by our staff. These include more flexibility towards staggered working hours and, where appropriate, the ability for some staff to work from home. We have been fully committed to equal opportunities for many years and continue to work hard to achieve a representative balance at all levels of staff through our "valuing diversity" initiative. The diversity of our workforce gives us a competitive advantage in dealing with today's global marketplace. As a core business value, diversity encourages innovation and a more productive team environment. Our diversity will enable us to keep pace with changing demographics, and to continue to attract and retain the best employees.

Outlook – 2002

As we are commencing the third year of our five-year strategic plan, we do not anticipate any changes in overall strategic direction for 2002. However emphasis is expected in the following areas:

- **Controlled growth in an environment of risk and uncertainty** – We continue to develop nationally, mainly through organic growth. In addition, opportunistic acquisitions will be considered. However, the risks and uncertainties in the economy will make 2002 a challenging year. As a result, business growth will be managed conservatively, maintaining the strict underwriting criteria that has enabled us to maintain credit losses below industry averages. We will continue to work closely with both our borrowing and investing clients to assist them in this volatile environment.
- **Continue to build on a solid financial foundation** – Despite the challenging market conditions, a difficult credit environment and weak capital markets, our balance sheet is strong, liquid, well capitalized and conservatively positioned.
- **Cost control** – We continue to look for ways of controlling or reducing costs and are particularly focused on improving the cost:income ratio by routing transactional services through appropriate alternative delivery channels. While our branch network will remain a critical delivery channel, we plan to expand the utilization of our telephone and Internet banking services. Capitalizing on the HSBC Group's economies of scale remains a priority.
- **Focus client activities in our areas of expertise** – We are focused on increasing penetration of our existing customer base by better understanding and meeting our clients' needs, and ensuring they have ready access to the full range of the HSBC Group's global products and services. Superior customer service is a key differentiator for HSBC in Canada and is considered a significant competitive advantage.
- **Build the "HSBC" brand in Canada** – The HSBC Group, through a global advertising campaign, is devoting further resources to increase Canadian awareness of the HSBC Group's global capabilities to enhance its market share. Additional high profile sponsorships have been committed for 2002 including the Vancouver Sun Run in April and the "HSBC Power Smart Celebration of Light" international fireworks festival later in the summer. In Toronto, we continue to be a 2002/2003 season sponsor for the Roy Thomson and Massey Halls. During the 2001/2002 winter, we sponsored "Kids Ski Free" at Blue Mountain, Collingwood, Ontario. The HSBC Group is one of the largest sponsors of the Canadian Formula One Grand Prix to be held in Montreal in June 2002, where the HSBC Group sponsored Jaguar Formula 1 racing team will be competing. We are participating in the HSBC Group's strategic alliance with the "Yahoo!™" "Pay Direct" payment system which we anticipate will launch in Canada in 2002.

The opening, in March 2002, of a Wholesale Banking branch by HSBC Bank USA in Toronto will assist us to leverage its larger capital base on behalf of our larger borrowing clients, resulting in additional business in Canada. In April 2002, our two branches in Seattle and Portland will be transferred to HSBC Bank USA as part of a strengthening of their West Coast network. This will further enhance our capabilities in serving customers in the important Pacific Corridor.

Analysis of financial results for the year ended December 31, 2001

HSBC recorded net income attributable to common shares for the year ended December 31, 2001 of $206 million, 21.9% higher than $169 million for 2000. Income before taxes and non-controlling interest in income of subsidiaries was $377 million for the year ended December 31, 2001, an increase of 8.6%, compared to $347 million for 2000.

The underlying business of HSBC performed strongly. There was improved profitability from all of our business lines despite the challenging economic environment, although there was an impact from increased provisions for credit losses. The return on equity was 14.9% for 2001, compared to 15.3% for 2000, due primarily to a higher level of retained capital.

For the year ended December 31, 2001 the cost:income ratio, excluding amortization of goodwill and intangible assets, improved by nearly 600 basis points to 59.3% compared to 65.2% for 2000.

Net interest income: Net interest income for 2001 was $754 million, up 13.2% over 2000. This increase was due to a combination of continuing growth in the loan and core customer deposit portfolios, primarily commercial loans and residential mortgages, together with higher spreads due to improved pricing and market conditions.

The improvement in net interest margin for the year resulted partly from a fall in funding costs as the cost of funds fell in advance of anticipated decreases in the Canadian prime and U.S. base lending rates. Net interest margin, as a percentage of average interest earning assets, for 2001 was 2.70%, 2 basis points higher than in 2000. Market spreads have been at or near record levels during 2001, with increases in Canadian prime/bankers' acceptance and US base/LIBOR spreads of more than 40 basis points during the year. However, the impact of these spread increases were reduced as the numerous rate decreases totaling more than 350 basis points during 2001 caused a reduction in the value of low cost and interest free funds, particularly in the last quarter.

Other income: Other income was $419 million compared to $462 million in 2000. The weakness in the global equity markets, experienced throughout 2001 resulted in lower capital market fees and trading revenue. Capital market fees for 2001 were $98 million compared to $162 million for 2000 which included $30 million of capital market fees from HSBC InvestDirect (Canada) Inc. ('InvestDirect') which was transferred to the Merrill Lynch HSBC joint venture in the fourth quarter of 2000.

Excluding capital market fees and trading revenue, income from the other lines of business, primarily personal and commercial financial services, increased 12.4% for 2001 compared to 2000. Revenue from credit services, principally income from bankers' acceptances, letters of credit and guarantees increased by 29.4%. Revenues from deposit and payment services increased by 15.2%. This was mainly due to increased use of our international payments services and an increased customer base. Despite the drop in global equity markets, mutual fund and administration fees increased by nearly 6.9%, mainly due to the increase in sales of HSBC Mutual Funds.

Non-interest expenses: Non-interest expenses decreased by 5.1% to $704 million compared with $742 million for 2000. Salaries and employee benefits were 6.8% lower, due primarily to lower performance-based compensation following the significant decrease in capital market fees and trading revenue. There were additional charges of $9 million for costs associated with headcount reductions in the fourth quarter of 2001. Premises and equipment expenses increased by 6.5% mainly due to increased computer charges. Other expenses decreased 7.6%, mainly due to a decrease in volume-driven transaction expenses resulting from the lower capital market income in 2001. In addition, corporate disciplines in cost controls resulted in reducing expenses in many overhead expense categories, although this was offset by a number of unusual operating expenses. The previous year also included $15 million of non-interest expenses from InvestDirect.

Provision for income taxes: The provision for income taxes was $147 million in 2001 compared to $155 million in 2000. The effective tax rate, which is computed from the income before taxes, less non-controlling interest in the income of subsidiaries, decreased 500 basis points to 40.7% from 45.7% in 2000. The major components of the decrease related to a lowering of combined federal and provincial tax rates, together with the decreased impact in 2001 of reductions in the value of future tax assets resulting from the lowering of future tax rates.

Credit quality and provision for credit losses: During 2001, the overall credit quality remained sound. The provision for credit losses increased to $92 million for the year ended December 31, 2001, compared to $39 million in 2000. The higher level of provisions for the year resulted from the deterioration in a small number of commercial facilities, and the maintenance of a level of general allowances consistent with the underlying risk portfolio of the loan book and stage of the credit cycle. Deteriorating economic conditions throughout North America during 2001 had a significant impact on many sectors of the economy, especially in those industries considered as part of the "New Economy." Increased corporate defaults were a feature of 2001. Against this background, our conservative approach to credit granting and proactive loan management helped mitigate these external factors. The allowance for credit losses exceeded gross impaired loans by $33 million at December 31, 2001 compared to $111 million at December 31, 2000. The ratio of general allowances to risk weighted assets reduced to 110 basis points at December 31, 2001 from 124 basis points at December 31, 2000, although the absolute level of the general allowance increased marginally to $235 million from $234 million.

Management's Discussion and Analysis (continued)

Balance sheet: Despite the challenging economic environment, HSBC achieved broadly based growth during 2001. Total assets at December 31, 2001 were $33.3 billion, up $3.8 billion (12.9%) from December 31, 2000. Loans and acceptances increased by $2.6 billion. During 2001 there was some growth in the commercial loan portfolio, which, including acceptances, grew 5.1%. However, significantly lower interest rates fuelled demand for residential mortgages, which grew by 10.7% before taking into account the effects of securitizations. During 2001, the acquisition of CCF Canada and Credit Lyonnais Canada was completed increasing assets by $64 million.

Total deposits increased $3.2 billion (13.6%) during 2001. Personal deposits grew $1.3 billion (10.5%) to $13.4 billion compared to $12.1 billion at December 31, 2000. Commercial deposits increased by $0.9 billion (8.4%) to $11.6 billion.

Funds under management: Funds under management increased 3.9% to $10.6 billion at the end of 2001, compared to $10.2 billion at December 31, 2000. These funds were comprised of $4.9 billion of brokerage clients' assets and $5.7 billion of portfolio management and mutual fund products. During 2001, portfolio management and mutual fund balances increased by 9.6% while brokerage clients' assets decreased by 2%. The increase in funds under management reflected strong growth in mutual funds, which more than offset the decline in market values due to the weak global equity markets over the year. These results are considered good in view of the difficult market conditions.

Quarterly Summary of Statements of Income

	2001				2000			
	Quarter ended				*Quarter ended*			
	Dec. 31	*Sept. 30*	*June 30*	*March 31*	*Dec. 31*	*Sept. 30*	*June 30*	*March 31*
	(unaudited, in millions)							
Net interest and other income	**$ 278**	**$ 274**	**$ 265**	**$ 264**	$ 285	$ 267	$ 271	$ 266
Total non-interest expenses	**197**	**171**	**172**	**164**	180	177	194	191
Income before taxes	**81**	**103**	**93**	**100**	105	90	77	75
Provision for income taxes	**(26)**	**(42)**	**(38)**	**(41)**	(61)	(36)	(30)	(28)
Non-controlling interest in income of subsidiaries	**(4)**	**(4)**	**(4)**	**(4)**	(4)	(4)	–	–
Net income	**51**	**57**	**51**	**55**	40	50	47	47
Preferred share dividends	**(2)**	**(2)**	**(2)**	**(2)**	(2)	(2)	(11)	–
Net income attributable to common shares	**$ 49**	**$ 55**	**$ 49**	**$ 53**	$ 38	$ 48	$ 36	$ 47

In the opinion of management, unaudited quarterly information contains all adjustments necessary for a fair presentation of such information. All such adjustments are of a normal and recurring nature.

Capital Management

HSBC manages its capital resources to ensure their efficient use in the generation of shareholder value while supporting business activities, including the asset base and risk positions, as well as providing prudent depositor security and complying with all applicable regulatory requirements.

HSBC's ultimate parent, HSBC Holdings, is strongly capitalized with a Tier 1 capital ratio of 9.0% and a total capital ratio of 13.0% at December 31, 2001. HSBC manages its capital in accordance with HSBC Holdings' corporate policies and external regulatory requirements. HSBC Holdings is regulated by the Financial Services Authority (United Kingdom).

Capital adequacy for Canadian federally incorporated financial institutions is regulated by the Superintendent of Financial Institutions Canada (the "Superintendent"). Their guidelines are based upon recommendations for capital adequacy standards provided by the Bank for International Settlements ("BIS"). Although the BIS currently continues to recommend that financial institutions maintain 4% and 8% Tier 1 and total capital ratios, respectively, the Superintendent recommended that Canadian banks maintain minimum Tier 1 and total capital ratios of 7% and 10%, respectively.

Tier 1 capital is the permanent capital of a bank, comprising common shareholders' equity, qualifying non-cumulative preferred shares, contributed surplus and retained earnings. Tier 2 capital includes subordinated debentures, general allowances and cumulative preferred shares. Total capital comprises both Tier 1 and Tier 2 capital. The tier 1 capital ratio was 8.6% and the total capital ratio was 11.3% at December 31, 2001. This compares with 8.6% and 11.5%, respectively, at December 31, 2000. The Superintendent permits HSBC to maintain an assets to capital multiple of up to 20 times.

Canada Deposit Insurance Corporation ("CDIC") has a tiered, differential insurance premium ratings system, which includes targets for capital adequacy. One of the measures CDIC uses in determining whether a financial institution is well capitalized is an assets (as defined by CDIC) to regulatory capital multiple. CDIC regards a financial institution as being well capitalized if it maintains an assets to regulatory capital multiple of less than 85% of the Superintendent's maximum permitted assets to capital multiple for each individual institution. HSBC targets to be prudently below CDIC's more conservative threshold of 17 times and at December 31, 2001, HSBC's multiple was 14.5 times.

HSBC has formal capital management policies, which have been approved by the Board of Directors and HSBC Holdings, and which have been reviewed by the applicable regulatory authorities. These capital management policies lay out a strict regime of capital monitoring, targets, limits and maintenance actions. HSBC Finance and Treasury departments manage compliance with the policies on a day-to-day basis, with weekly monitoring by HSBC's Asset and Liability Committee ("ALCO"). ALCO is chaired by the Chief Financial Officer and includes the Chief Executive Officer, Chief Operating Officer and certain other senior executives, including those responsible for credit, risk management, marketing and sales, operations and treasury.

HSBC employs well-developed personal and commercial relationship management performance measurement tools to ensure that shareholder capital is efficiently deployed by its major business segments. These tools measure the value added by each customer relationship against the capital required to support the risk-taking facilities granted. Capital necessary to support customers is determined according to the various requirements of the Superintendent, CDIC and BIS noted above.

HSBC monitors and adopts techniques in capital management, managing the dynamic of maximizing shareholder value against the fundamental need to be prudently capitalized.

Management's Discussion and Analysis (continued)

Regulatory Capital Ratios

HSBC's regulatory capital and capital adequacy ratios and its assets to capital multiple are as follows:

	As at December 31	
	2001	2000
	(in millions, except ratios)	
Tier 1 Capital		
Common shares	**$ 935**	$ 935
Contributed surplus	**165**	165
Retained earnings	**387**	181
Non-cumulative preferred shares	**125**	125
Non-controlling interests in subsidiaries[1]	**230**	230
Goodwill	**(6)**	(7)
Total Tier 1 capital	**1,836**	1,629
Tier 2 Capital		
Subordinated indebtedness (net of amortization)	**406**	410
General allowance for credit losses	**186**	140
Total Tier 2 capital	**592**	550
Total Tier 1 and Tier 2 capital	**2,428**	2,179
Securitization-related deductions[2]	**(7)**	(5)
Total capital available for regulatory purposes	**$ 2,421**	$ 2,174
Total risk-weighted assets	**$ 21,416**	$ 18,901
Regulatory Capital Ratios		
Tier 1 capital	**8.6%**	8.6%
Total capital	**11.3%**	11.5%
Assets to capital multiple	**14.5x**	14.2x

(1) *Includes $200 million of innovative tier 1 HSBC Canada Asset Trust Securities (HSBC HaTS).*

(2) *As at December 31, 2001, HSBC utilized $3 million of general allowances for credit losses to lower the reduction from capital for securitization issues such as first loss protection.*

Risk-weighted Assets

Risk-weighted assets requiring capital support arise from the provision to customers of credit and other risk facilities. Risk-weighted assets are determined by HSBC by applying the specific weighting factors provided by the Superintendents' capital adequacy guidelines. HSBC's risk-weighted assets are as follows:

	As at December 31	
	2001	2000
	(in millions)	
On-Balance Sheet Assets		
Cash resources	**$ 696**	$ 439
Securities	**286**	262
Mortgage loans	**3,826**	3,207
Other loans	**12,172**	11,177
Acceptances	**2,571**	2,134
Other assets	**524**	615
Total on-balance sheet assets	**20,075**	17,834
Off-Balance Sheet Instruments		
Guarantees and letters of credit	**888**	786
Other	**281**	172
Subtotal	**1,169**	958
Derivatives[1]	**172**	109
Total off-balance sheet instruments	**1,341**	1,067
Total risk-weighted assets	**$ 21,416**	$ 18,901

(1) *Derivatives are stated at their risk weighted equivalent.*

Regulatory Capital Generation

HSBC's regulatory capital generation is as follows:

	As at December 31	
	2001	2000
	(in millions)	
Internally Generated Capital		
Net income	**$ 214**	$ 184
Gain on sale of HSBC InvestDirect (Canada) Inc.	**–**	88
Capital from operations	**214**	272
Dividends	**(8)**	(825)
General allowance for credit losses	**46**	19
Other	**(1)**	11
	251	(523)
External Financing		
Issue of common equity	**–**	860
Subordinated indebtedness (net of amortization)	**(4)**	18
Preferred shares issued	**–**	125
Preferred shares redeemed	**–**	(270)
Issue of innovative instruments included in Tier 1 capital	**–**	200
Total increase in regulatory capital	**$ 247**	$ 410

There has been no externally raised regulatory capital in 2001. As a result of the 2001 acquisition of CCF Canada, HSBC did acquire a third party subordinated debenture. However, the debenture is due for repayment in 2002 and does not qualify as tier 2 regulatory capital. Effective December 31, 2001, the Superintendent increased the inclusion rate for general allowances in tier 2 capital to 87.5 basis points of risk weighted assets from the previous maximum of 75 basis points. This added $27 million to regulatory capital in addition to the $19 million added through organic growth.

In 2000, HSBC completed concurrent public offerings of $125 million of class 1 Preferred Shares Series A and $200 million HSBC HaTS (Asset Trust Securities issued by HSBC Canada Asset Trust). The aggregate proceeds received by HSBC from the issue and sale of the Class 1 Preferred Shares Series A to the public and from the sale of the initial trust assets to HSBC Canada Asset Trust were approximately $320 million, net of issue costs of $4 million. HSBC used $270 million of these proceeds to redeem all of the issued and outstanding Class 2 Preferred Shares Series A held by an affiliate and the balance was used for general corporate purposes. There was a further increase issue of common shares in August 2000 of $100 million.

As a result of a corporate restructuring within the HSBC Group, in November 2000 HSBC paid a dividend of $810 million on its common shares and received proceeds of $760 million on the issue of additional common shares. No dividends were paid on common shares in 2001.

Risk Management

All business activities require the management of particular risks or combinations of risks. Risk management is the identification, analysis, evaluation and management of the factors which could adversely affect HSBC's resources, operations and financial results. The risk factors most likely to affect HSBC are credit, market, liquidity and operational risks. HSBC believes it conservatively manages its exposure to these risk factors. Formal risk management policies have been established which identify and analyze these risk elements and set appropriate risk limits. HSBC continually monitors these risks and limits them by means of internal control measures which management considers are up to date and reliable.

HSBC reviews and modifies its risk management policies and systems regularly to reflect changes within HSBC and within the markets in which it operates. The Board of Directors approves HSBC's risk management policies. HSBC's overall risk management limits are set, taking into account HSBC Holdings' overall risk limits. ALCO monitors and reviews risk positions against prescribed limits.

Management's Discussion and Analysis (continued)

Credit Risk Management

Credit risk arises when reliance is placed on a counterparty to honour contractual obligations arising out of credit granting, credit substitutes (such as letters of credit and guarantees) and contingent risk relating to derivative contracts such as forward foreign exchange contracts and interest rate swaps. Concentration of credit risk may arise when the ability of a number of counterparties to meet their contractual obligations are similarly affected by external factors. Examples of concentration risk would include geographic, industry or environmental factors. Therefore, diversification of credit risk is a key concept by which HSBC is guided.

Credit limits are established after consultation with HSBC Holdings and are approved by the Board of Directors. All credit exposure is subject to a credit approval and review process approved by the Board of Directors. Credit authorities are delegated to senior credit management, who in turn delegate to line management. Credit exposures in excess of certain levels may require the concurrence of HSBC Holdings.

The Board of Directors and the Credit Committee of the Board meet quarterly to review portfolio credit quality, geographic, product and industry distributions, large customer concentrations and adequacy of loan provisions. Policies relating to large customer concentration and industry, product and geographic distribution are approved by the Board in line with HSBC Group policy. All new major authorized facilities, derivative exposure and special credit problem facilities are also reviewed quarterly by the Credit Committee of the Board. The appetite for credit risk is expressed through Commercial and Personal Lending Guidelines which are approved quarterly by the Credit Committee of the Board and disseminated throughout HSBC.

There is a disciplined approach to managing credit risk through ongoing monitoring of all credit exposures at branches, and by the credit and internal audit departments. Credits that do not meet the lending guidelines are approved on an exception basis and problem and impaired loans are identified at an early stage and actively managed by a separate dedicated Special Credit management unit. Segmentation of credit risk is ensured through a formal and strictly maintained risk grading system that is assigned to all clients and monitored closely to ensure changes in credit risk are reflected by the appropriate credit grade. Credit scoring and related bureau-based management techniques along with judgmental management are used to manage risk associated with consumer clients.

Real estate lending is managed within well-defined parameters with an emphasis on relationship and project sponsorship for all new transaction. Appraisal policy is approved annually by the Board of Directors and an approved list of appraisers is maintained to ensure conservative and consistent valuation of real estate collateral. Environmental risk is managed through the use of approved consultants to provide opinions wherever environmental risk is identified.

A review of all credit matters undertaken by branch and head office credit managers is completed regularly by internal auditors to ensure that all policies, guidelines, practices, conditions and terms are followed. Management believes adequate internal controls are in place to establish and maintain the credit quality of the financial assets.

Loan Portfolio

In assessing its loan portfolio, HSBC includes all of its credit exposures, including customers' liabilities under acceptances, guarantees and letters of credit. The following is an analysis of the constituents of the portfolio:

	As at December 31	
	2001	2000
	(in millions)	
Loans included in financial statements, net of allowances	**$ 21,870**	$ 19,753
Allowance for credit losses	**315**	285
Customers' liabilities under acceptances	**2,571**	2,134
Letters of credit	**469**	408
Guarantees	**1,169**	970
Total loans	**26,394**	23,550
Non-performing loans	**(282)**	(174)
Total performing loans	**$ 26,112**	$ 23,376

The performing loan portfolio is comprised of commercial, personal and residential mortgage loans with an approximate split between commercial and personal loans (including residential mortgages) of 60% to 40%. The geographic distribution of the loan portfolio at December 31, 2001 was British Columbia (46.9%), Ontario (26.9%), Western Canada (including Alberta, Saskatchewan and Manitoba) (13.9%) and the Quebec and Atlantic Region (10.4%).

Performing commercial loans at December 31, 2001 aggregated $15.5 billion and were distributed across various industry sectors with the highest concentrations in real estate (27.4%), wholesale/retail trade (23.3%) and service industries (18.7%). Large customer concentrations are borrowing groups where approved facilities exceed 10% of the regulatory capital base. As at December 31, 2001, 10% of HSBC's regulatory capital base amounted to approximately $242 million.

The following tables, in which commercial includes customers' liabilities under acceptances, letters of credit and guarantees, provide details of the overall performing loan portfolio, and geographic distribution, industry distribution and large customer concentration:

Performing Loan Portfolio

	As at December 31			
	2001		2000	
	(in millions, except ratios)			
Consumer loans	**$ 2,220**	**8.5%**	$ 1,885	8.1%
Residential mortgages	**8,353**	**32.0%**	6,785	29.0%
Total consumer	**10,573**	**40.5%**	8,670	37.1%
Total commercial	**15,539**	**59.5%**	14,706	62.9%
Total performing loans	**$ 26,112**	**100.0%**	$ 23,376	100.0%

Performing Loan Portfolio
Geographic Distribution

	As at December 31			
	2001		2000	
	(in millions, except ratios)			
British Columbia	**$ 12,257**	**46.9%**	$ 11,183	47.8%
Western Canada	**3,623**	**13.9%**	2,872	12.3%
Ontario	**7,032**	**26.9%**	6,194	26.5%
Quebec and Atlantic	**2,713**	**10.4%**	2,685	11.5%
US Branches	**487**	**1.9%**	442	1.9%
Total performing loans	**$ 26,112**	**100.0%**	$ 23,376	100.0%

Performing Commercial Loan Portfolio
Industry Distribution

	As at December 31			
	2001		2000	
	(in millions, except ratios)			
Real estate	**$ 4,254**	**27.4%**	$ 4,007	27.2%
Hotels and hospitality	**988**	**6.4%**	968	6.6%
Trade	**3,623**	**23.3%**	3,148	21.4%
Services	**2,907**	**18.7%**	3,157	21.5%
Manufacturing	**2,224**	**14.3%**	2,015	13.7%
Other	**1,543**	**9.9%**	1,411	9.6%
Total commercial loans	**$ 15,539**	**100.0%**	$ 14,706	100.0%
As a percentage of total performing loans	**$ 26,112**	**59.5%**	$ 23,376	62.9%

Management's Discussion and Analysis (continued)

Performing Commercial Loan Portfolio
Large Customer Concentration

	As at December 31	
	2001	2000
	(in millions, except ratios)	
Large customer concentration	**$ 2,460**	$ 2,140
As a percentage of total commercial loans	**15.8%**	14.6%
As a percentage of total performing loans	**9.4%**	9.2%

Credit Quality

HSBC categorizes the credit quality of its loan portfolio as follows:

- *Satisfactory* – Borrower's financial condition and future capacity to repay is considered satisfactory.
- *Watch* – Borrower's financial condition has shown sustained or continued deterioration and requires frequent monitoring. The capacity to repay remains satisfactory.
- *Sub-standard* – Borrower's financial condition is weak. However, it is still expected that full repayment will be received.
- *Impaired* – Loans are considered impaired if an amount is contractually 90 days in arrears or management is of the opinion that there is no longer reasonable assurance as to the ultimate collectibility of all or some portion of principal or interest. Impaired loans are classified as non-performing. Specific provision is made for any anticipated loss.

The following table sets forth an analysis of the total loan portfolio on the basis of the above credit quality categories:

Performing and Non-Performing Loan Portfolio

	As at December 31			
Credit Quality	**2001**		2000	
	(in millions, except ratios)			
Satisfactory	**$ 24,878**	**94.3%**	$ 22,407	95.1%
Watch	**923**	**3.5%**	671	2.9%
Sub-standard	**311**	**1.2%**	298	1.3%
Impaired	**282**	**1.0%**	174	0.7%
Total loans	**$ 26,394**	**100.0%**	$ 23,550	100.0%

Greater than 94% of the total loan portfolio is categorized as satisfactory. Credit quality of the portfolio has remained stable over the past five years. As at December 31, 2001, $282 million (1.0%) of the loan portfolio was impaired, with specific and general allowances providing 112% (December 31, 2000 - 164%) coverage of these loans.

Impaired Loans and Allowances

Allowances for credit losses are maintained at a level to absorb all estimated credit-related losses in the portfolio, which may arise from both on and off balance sheet credit exposures. These exposures include deposits with other regulated financial institutions, loan substitute securities, loans, acceptances, derivative instruments and other credit-related contingent liabilities, such as letters of credit and guarantees.

Assessing the adequacy of the allowance for credit losses is inherently subjective as it requires making estimates, including the amount and timing of expected future cash flows, that may be susceptible to significant change. Specific allowances are recorded on a loan-by-loan basis for those loans where management believes the ultimate collectibility of all or some portion of principal or interest is in doubt, to reduce the book value to expected recovery level. The level of specific allowances are determined on an individual asset basis for all commercial loans and some personal loans, while a formula approach is utilized for personal loans with similar characteristics. A number of methods are used in determining specific allowances including discounted value of future cash flows, observable market values or the fair values of the underlying security. Impaired loans are reviewed at least quarterly and the appropriate specific provisions are recorded based on estimated net realizable amounts.

The general allowance represents management's best estimate of probable losses within the portion of the portfolio that have not yet been specifically identified as impaired.

On October 31, 2001, the Superintendent's office released its final Guideline C-5 "General Allowances for Credit Risk", effective for fiscal years commencing after November 1, 2001. In line with this guideline, HSBC has established a methodology for management's use in establishing general allowances. The methodology involves the application of expected loss factors to outstanding facilities. The general allowance for large business and government loans and acceptances in the model is based on the application of expected default and loss factors. For more homogeneous portfolios, such as residential mortgages, small and mid market business loans and personal loans, the determination of the general allowance is done on a product portfolio basis. The losses are determined by the application of loss ratios determined through the analysis of write-off trends over an economic cycle, adjusted to reflect changes in the product offerings and credit quality of the pool. Also included are portfolio adjustments that include consideration of general economic and business conditions, recent loan loss experience and trends in credit quality and concentrations, particularly where experience is considered low in relation to the industry as a whole. This allowance also reflects model and estimation risk, but does not represent future losses. In establishing the amount of general allowances management has been guided by this methodology.

The following table provides details of the impaired loan portfolio:

Impaired Loan Portfolio	As at December 31 **2001**	As at December 31 2000
	(in millions)	
Commercial		
Real estate	$ **82**	$ 41
Manufacturing	**34**	24
Trade	**38**	36
Services	**12**	14
Other	**79**	21
Total commercial loans	**245**	136
Personal		
Consumer loans	**13**	14
Residential mortgages	**24**	24
Total personal loans	**37**	38
Total impaired loans	$ **282**	$ 174
Specific allowances	$ **80**	$ 51
General allowances	**235**	234
Total allowance for credit losses	$ **315**	$ 285
Net impaired loans	$ **(33)**	$ (111)

The following table shows the coverage of specific allowances as a percentage of the related impaired loans:

Coverage by Specific Allowance	As at December 31 **2001**	As at December 31 2000
Commercial real estate	**12%**	34%
Commercial manufacturing	**29%**	33%
Commercial other	**38%**	27%
All commercial	**28%**	30%

Management's Discussion and Analysis (continued)

The following table sets out the coverage of general provisions as a percentage of total performing loans and risk-weighted assets. In view of an improving geographic and industry concentration, and past low loan loss experience, a slight decline in the coverage as a percentage of risk-weighted assets is considered acceptable. The general allowance represents the best estimate of probable losses within the portfolio that have not yet been specifically identified as impaired:

	As at December 31	
Coverage by General Allowance	**2001**	2000
As a percentage of total performing loans	**0.90%**	1.00%
As a percentage of risk-weighted assets	**1.10%**	1.24%

Provisions for Credit Losses

The following table sets out the provisions for credit losses charged to the consolidated statements of income. Specific provisions have increased due to the deterioration of a small number of commercial credit facilities:

	As at December 31	
	2001	2000
	(in millions, except percentages)	
Specific provisions	**$ 84**	$ 28
General provisions	**8**	11
Total provision for credit losses	**$ 92**	$ 39
Specific provisions as a percentage of total loan portfolio	**0.32%**	0.12%

Derivative Portfolio

The credit equivalent amount of derivative exposure is established by the current replacement cost of positions plus an allowance for future fluctuation of derivative contracts. Derivatives are entered into primarily to support customer requirements and to assist HSBC in its management of assets and liabilities. The credit equivalent amount of the derivative portfolio by product type is as follows:

	As at December 31	
Products	**2001**	2000
	(in millions)	
Interest rate contracts	**$ 182**	$ 80
Foreign exchange contracts	**474**	338
Equity contracts	**12**	11
Total	**668**	429
Impact of master netting agreements	**(92)**	(27)
Net credit equivalent amount	**$ 576**	$ 402

Market Risk Management

Market risk is the potential that interest rates, foreign exchange rates or equity prices will move and impact earnings. Market risk arises on financial instruments that are valued at market prices and on those instruments valued at cost plus accrued interest.

HSBC makes markets in interest rate, exchange rate and equity derivative instruments, as well as in debt, equity and other securities. Trading risks arise either from customer-related business or principal investing activities.

Market risk is managed through risk limits set out by ALCO and approved by the Board of Directors.

Risk limits are determined for each portfolio and are set by product and risk type, with market liquidity being a principal factor in determining the levels of limits set. Limits are reviewed annually using a combination of risk measurement techniques including present value of a basis point (PVBP), value at risk (VaR), foreign exchange exposure limits, maximum loss limits, options premium paid limits and product and issuance limits.

PVBP is a sensitivity measure which calculates the impact on the present value of a transaction (or a portfolio of transactions) of a one basis point movement in rates. VaR is a statistical technique which estimates the potential losses that could occur on risk positions taken due to movements in market rates and prices over a specified time horizon and to a given level of confidence.

Risk limits are set for each operation and are dependent upon the size, financial and capital resources of the entity, market liquidity of the instruments traded, business plan, experience and track record of management and dealers, internal audit gradings, support function resources and computer systems. Risk limits are reviewed and set on an annual basis.

Interest Rate Risk

Interest rate risk arises primarily out of differences in the term to maturity or repricing of the assets and liabilities both on and off balance sheet. These interest rate risk exposures, or "gaps", are monitored by ALCO on a weekly basis against prescribed limits. The gap position measures assets and liabilities based on contractual repricing data as well as incorporating assumptions on customer behaviour on products with a degree of optionality as to prepayment, redemption or repricing (such as redeemable deposit products and mortgages with prepayment options). These assumptions, which are based on historical behavioural patterns, are periodically reviewed by ALCO.

HSBC believes it takes a conservative approach in setting limits on these mismatched positions. Limits are established based on the impact on net interest income of an immediate and parallel upward shift in the relevant yield curves of one percent. HSBC also has established limits on these mismatched positions in terms of Dollars at Risk, VaR and PVBP.

A variety of cash and derivative instruments (principally interest rate swaps) are used to manage interest rate risk. Derivatives are used to modify the interest rate characteristics of related balance sheet instruments and to hedge anticipated exposures when market conditions of price and liquidity are considered beneficial.

Interest rate risk also arises in the fixed income trading activities. Limits have been established in terms of VaR, PVBP, maximum loss limits, product and issuance limits, and premium paid limits for option contracts.

Foreign Exchange Risk

Foreign exchange risk arises from foreign currency denominated asset and liability positions taken by HSBC. HSBC buys and sells currencies in the spot, forward, futures and options markets, on behalf of its customers and for its own account, to manage its own currency exposures arising from assets and liabilities denominated in currencies other than the Canadian dollar. Limits have been established as to the magnitude of the exposure on a currency-by-currency basis as well as maximum loss limits on any position held.

Equity Risk

Equity risk arises as a result of movements in the price of equity positions taken and held principally by HSBC Securities. Limits have been established in terms of permitted instruments, open positions, notional aggregate long or short positions, maximum loss limits, single stock limits, premium paid limits and currency limits.

Liquidity Risk Management

HSBC manages the liquidity structure of its assets, liabilities and commitments so that cash flows are appropriately balanced and all funding obligations are met when due. HSBC also ensures compliance with Canadian regulatory requirements. Treasury department manages liquidity on a day-to-day basis.

ALCO oversees compliance with liquidity requirements on a weekly basis by monitoring:

- projected cash flows and the levels of related liquid assets,
- specified balance sheet liquidity ratios against prescribed limits,
- depositor concentration in terms of overall funding mix and to avoid undue reliance on large individual and non-core depositors, and
- liquidity contingency plans.

Customer deposits form a significant portion of overall funding. Considerable importance is placed on the stability and growth of this core deposit base. Capital markets are accessed for the purposes of providing additional funding, maintaining a presence in the marketplace and aligning asset and liability maturities.

Management's Discussion and Analysis (continued)

Limits have been established for balance sheet ratios and minimum periods of forecast positive cumulative cash flow as well as contingencies to meet cash flow needs.

Operational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

Operational risk is managed through disciplined application and evaluation of internal controls, appropriate segregation of duties, independent authorization of transactions and reconciliation and monitoring of transactions on a regular and systematic basis. These processes are supported by an independent program of periodic reviews undertaken by the Internal Audit department. Contingency facilities are also maintained to support operations in the event of a disaster. Daily settlement limits are also maintained to ensure that the exposure to counterparties is kept at an acceptable level, assisted by certain transfer systems, such as the large value transfer system, which assure finality of payment for individual transactions.

Analysis of Financial Results and Operations by Business Segments

The following is a summary of selected consolidated financial information and other data for each of HSBC's major business segments:

	Year ended December 31, 2001				
	Personal financial services	*Commercial financial services*	*Corporate and institutional banking*	*Treasury and markets*	*Total*
			(in millions, except ratios)		
Net interest income	**$ 326**	**$ 361**	**$ 30**	**$ 37**	**$ 754**
Other income	**182**	**164**	**25**	**48**	**419**
Total net interest income and other income	**$ 508**	**$ 525**	**$ 55**	**$ 85**	**$ 1,173**
Net income[(1)]	**$ 84**	**$ 102**	**$ 25**	**$ 30**	**$ 241**
Percentage of total net income	**34.9%**	**42.3%**	**10.4%**	**12.4%**	**100.0%**
Average assets	**$ 9,981**	**$ 12,685**	**$ 2,447**	**$ 6,734**	**$ 31,847**
Percentage of total average assets	**31.3%**	**39.8%**	**7.7%**	**21.2%**	**100.0%**

(1) *Before unallocated corporate expenses of $27 million, net of income taxes.*

	Year ended December 31, 2000				
	Personal financial services	*Commercial financial services*	*Corporate and institutional banking*	*Treasury and markets*	*Total*
			(in millions, except ratios)		
Net interest income	$ 300	$ 312	$ 24	$ 30	$ 666
Other income	211	152	17	82	462
Total net interest income and other income	$ 511	$ 464	$ 41	$ 112	$ 1,128
Net income[(1)]	$ 70	$ 96	$ 17	$ 29	$ 212
Percentage of total net income	33.0%	45.3%	8.0%	13.7%	100.0%
Average assets	$ 9,287	$ 11,061	$ 2,193	$ 5,942	$ 28,483
Percentage of total average assets	32.6%	38.8%	7.7%	20.9%	100.0%

(1) *Before unallocated corporate expenses of $28 million, net of income taxes.*

Personal Financial Services

Client Base. Personal Financial Services provides services to individuals through a segmented approach to understanding and meeting customer needs. Similarly, sales management maintains a balanced approach, focused on meeting clients' needs. To build on customer satisfaction, in 2001 and throughout 2002, emphasis has and will continue to be placed on developing people and systems infrastructure to improve relationship management and effectiveness of cross-selling.

Products and Services. Personal Financial Services offers a comprehensive range of financial products and services, including the following:

Personal Banking	*Asset Management*	*Brokerage*	*Insurance*	*Trust and Advisory*
Deposits and personal chequing accounts	Mutual funds	Full service (Self directed through Merrill Lynch HSBC)	Auto	Estate planning
Residential mortgages	Segregated funds		Home	Wills
Lines of credit	Personal portfolio management		Creditor	Investment administration
Personal loans			Travel	Executor and trustee services
Investments				
Credit cards				
Telephone and Internet banking				
Private client services				
HSBC *Premier*				
Retirement products				

Delivery Channels. HSBC provides personal financial products and services through over 160 offices, including 120 branches, as well as ABMs, direct debit and other electronic delivery channels such as the internet and telephone call centres. Although the branch network remains our key delivery channel, we continue to invest in, and grow, our direct client acquisition capabilities, third party deposit and loan broker channels and outbound calling capabilities. These were substantially expanded in 2001, including the opening of centralized processing centres.

We are growing our individual client base and market share using a segmented approach to meet client needs. This is achieved by ensuring clients with more extensive requirements receive a greater level of advisory service and by encouraging clients with more conventional transactions to utilize those delivery channels that most conveniently meet their needs. For example, private banking, through a relationship manager, provides targeted clients with a full complement of investment funds and services to plan, manage and protect their assets. Global Private Client Service was launched in 2001 in Vancouver and Montreal, with fully integrated wealth management centres combining Private Banking, Investment and Trust services for private segment clients. Further expansion is expected in 2002.

HSBC *Premier* is a clear example of our segmented and customer driven approach to products and services development. This worldwide service for the HSBC Group's most valuable personal customers operates in 17 countries and territories including Canada. HSBC *Premier* provides an exclusive suite of banking, credit and investment services and special privileges. Relationship management is a vital part of the HSBC *Premier* service, with dedicated relationship managers or teams responsible for facilitating everyday transactions and helping to satisfy the wider financial needs of the customer. HSBC *Premier* customers have exclusive access to dedicated HSBC *Premier* centres in selected locations in Canada, and over 100 centres located around the world. In addition to the 24-hour call centre support, a global travel assistance service is also available around the clock.

The Internet is becoming an increasingly vital tool for the delivery of the priorities set out in our strategy, especially in personal financial services. Customer Internet offerings are designed to meet three criteria: they must integrate with and complement our existing distribution channels; customer needs and preferences must be paramount; and what we offer must be international in scope. Use of our Internet Banking service, which was ranked the Number 2 bank in Canada in terms of ease of use by Gomez Canada in their fall 2001 survey, has shown encouraging growth. By the end of 2001, 12% of our customer base, representing a 400% increase over 2001, had registered. Our service will shortly be upgraded to further enhance functionality. A redesign of in-branch and online account opening procedures is anticipated to further improve ease of sign up.

Management's Discussion and Analysis (continued)

HSBC Mutual Funds, managed through our subsidiary HSBC Asset Management (Canada) Limited, is the third fastest growing family among the top 30 mutual fund companies in Canada ranked by size of assets. In 2001, our mutual fund assets grew by 16.4% over 2000 compared to 1.2% for the "top 30" group. In the December 2001/January 2002 edition of "MoneySense" magazine, an industry periodical, HSBC Mutual Funds were ranked as the best Bank-owned mutual fund family in Canada, and the 4th best overall. Ranking was based on the variety of funds, investment performance, cost and investor reward. HSBC Mutual Funds, which are now available in both US and Canadian dollars, can be distributed as load and no load funds, as well as through fee based financial advisors.

HSBC Securities provides local clients with a complete range of highly personalized investment and brokerage services, through more than 130 retail investment advisors located in cities across Canada supported by a global network of research analysts.

Our strategic partner Merrill Lynch HSBC, provides on-line, real time trading on stock exchanges in North America and Hong Kong SAR through Internet delivery capability, and also accepts telephone orders, through the company's global toll-free telephone network. It can deliver service for all major exchanges in Europe, North America and the Asia-Pacific region. Customers benefit from the strategic combination of Merrill Lynch's worldwide investment capabilities and award-winning research team together with the HSBC Group's global presence, client relationships and processing capabilities. In November 2001, Merrill Lynch HSBC Canada, was ranked joint second best discount broker in Canada by "Canadian Business" magazine. The financial position and operating results of Merrill Lynch HSBC Canada Inc. are not consolidated with those of HSBC.

Home and auto insurance is delivered on a direct sale basis to residents of British Columbia and Alberta through HSBC Canadian Direct Insurance Incorporated. During 2001, Canadian Direct Insurance was rebranded to HSBC Canadian Direct adopting the HSBC Group's "Hexagon" as its logo.

Selected Financial Information and Analysis. The following sets out selected consolidated financial information and other data for Personal Financial Services:

	Year ended December 31	
	2001	2000
	(in millions, except ratios)	
Net interest income	**$ 326**	$ 300
Provision for credit losses	**(20)**	(11)
Other income	**182**	211
Non-interest expenses	**(341)**	(372)
Income before the under noted:	**147**	128
Provision for income taxes	**(58)**	(56)
Non-controlling interest in income of subsidiaries	**(5)**	(2)
Net income	**$ 84**	$ 70
Average assets	**$ 9,981**	$ 9,287
Cost:income ratio	**67.1%**	72.8%

Personal financial services contributed $84 million (34.9%) to total net income for the year ended December 31, 2001, before unallocated corporate expenses. With $10.0 billion in average assets, Personal financial services represented 31.3% of total average assets for 2001.

For the year ended December 31, 2001, net income before taxes from Personal financial services increased 14.8% to $147 million compared to $128 million for 2000. Net interest income in 2001 benefited from strong growth in residential mortgages and consumer loans and a reduction in funding costs. The increase in provisions mainly represented an increase in delinquencies in the consumer loan portfolio. Other income for 2001 was lower than the comparable period in 2000 due to poor equity market conditions and the loss of income from InvestDirect, although there was a corresponding reduction in performance-based compensation and transaction-related expenses. Lower costs also resulted from reductions in corporate expenditures through increased efficiencies.

Commercial Financial Services

Client Base. Commercial financial services, which includes our middle market business, is one of our traditional strengths. We serve a wide range of customers, from sole proprietors to publicly listed companies. HSBC is a popular choice for commercial customers that are looking for a comprehensive range of financial services, and excellent customer service.

Products and Services. Commercial financial services provides credit, cash management, treasury, trade finance, investment banking and other financial services and products to businesses in Canada, including the following:

Commercial and Corporate Banking	*Asset Management*	*Investment Banking*	*Merchant Banking*	*Treasury*	*Trade Finance*
Lines of credit Term financing Deposits Cash management Leasing Merchant card services and point of sale terminals Business Internet Banking Hexagon Creditor life insurance	Portfolio and fund management Group RRSP Mutual funds	Corporate finance Mergers and acquisitions Advisory	Mezzanine finance Subordinated debt Working capital Private equity	Foreign exchange Deposits Fixed income Derivatives	Import and export finance

Delivery Channels. HSBC provides commercial financial services through commercial branches and subsidiary offices, including those of HSBC Securities, HSBC Capital and HSBC Asset Management, as well as through HSBC Group offices in 80 other countries and territories. Other delivery channels include the Internet, PC and telephone banking. The HSBC Group's proprietary global payments and cash management platform, Hexagon, enables electronic account balance and transaction information, transfer of funds, bill payments and processing of trade finance documents.

Commercial financial services customers are assigned a relationship manager to facilitate their interface with the HSBC Group both locally and internationally. HSBC also offers specialized relationship managers for professional partnerships and owner/operators in key markets. This decentralized approach has resulted in responsiveness and flexibility in the credit approval process, a factor which HSBC believes is a significant competitive advantage.

We offer a wide range of high quality cash management services that enable our customers to manage their local and international needs. Whatever the nature and location of our customers business, they enjoy the benefits of our local expertise backed by our international cash management teams.

In 2001, we received strong third party endorsement of our excellent customer service when the respondents to the Canadian Federation of Independent Business survey (Banking on Entrepreneurship, March 2001) ranked HSBC first among Canadian banks for "understanding my business". HSBC's trade finance operations continue to be a market leader, particularly for import letters of credit. In 2001, HSBC Holdings won the 'Best trade documentation bank' award from "Project and Trade Finance Magazine" for the 6th consecutive year. Leveraging the HSBC Group's worldwide network, trade finance has traditionally been, and continues to be a key competitive strength of HSBC.

HSBC recognizes that our customers often do business outside of Canada. Therefore, our employees work closely with colleagues in various countries to create effective solutions for customers' doing business cross border, particularly in the key southern Ontario market and in the Pacific corridor, as well as other countries in which the HSBC Group operates.

HSBC continues to enhance its commercial electronic banking channels to complement its branch network. The first Internet Banking platform designed for professional clients, sole proprietors and small commercial enterprises was launched in December 2001. Take up has been very positive to date and is expected to be strong throughout 2002. A comprehensive Business Internet Banking system offering payment and cash management services, international trade, enhanced access control and digital authentication is being developed and is expected to be launched in 2002. Automated credit scoring and management tools are also being developed to improve customer service and to enhance efficiency and productivity.

Management's Discussion and Analysis (continued)

Selected Financial Information and Analysis. The following sets out consolidated financial information and other data for Commercial Financial Services:

	As at December 31	
	2001	2000
	(in millions, except ratios)	
Net interest income	**$ 361**	$ 312
Provision for credit losses	**(68)**	(25)
Other income	**164**	152
Non-interest expenses	**(277)**	(263)
Income before the under noted:	**180**	176
Provision for income taxes	**(70)**	(76)
Non-controlling interest in income of subsidiaries	**(8)**	(4)
Net income	**$ 102**	$ 96
Average assets	**$ 12,685**	$ 11,061
Cost:income ratio	**52.8%**	56.7%

Commercial financial services increased profitability in 2001 contributing $102 million (42.3%) to total net income for the year ended December 31, 2001, before unallocated corporate expenses. With $12.7 billion in average assets, Commercial financial services represented 39.8 % of total average assets for 2001.

For the year ended December 31, 2001, net income before taxes from commercial financial services increased 2.3% to $180 million compared to $176 million for 2000. Net interest income in 2001 was higher due to continued growth in the commercial loan portfolio and the benefit of lower funding costs. Offsetting this was a higher provision for credit losses covering a small number of deteriorating facilities. Other income in 2001 was higher overall than 2000 resulting from increased credit fees and trade finance income. Continued weak equity markets impacted capital market revenue, although this also resulted in lower variable compensation and processing expenses. Corporate efficiencies also benefited costs.

Corporate and Institutional Banking

Client Base. Corporate and Institutional Banking provides a comprehensive range of financial services to the HSBC Group's large multinational clients. Corporate and Institutional Banking is focused on entities that have a need for global value added products through investment banking, structured lending and trade services.

Products and Services. Corporate and Institutional Banking provides the following products and services:

Corporate Banking	*Asset Management*	*Investment Banking*	*Treasury*	*Trade Finance*
Lines of credit Term financing Deposits Payments and cash management Leasing	Portfolio and fund management Group RRSP	Corporate finance Mergers and acquisitions Advisory	Foreign exchange Deposits Fixed income Derivatives	Import and export finance

Delivery Channels. HSBC provides Corporate and Institutional Banking services through its principal branches and subsidiary offices, coordinated with HSBC Group worldwide operations. The HSBC Group's proprietary international payments and cash management platform, *Hexagon*, is linked electronically to HSBC Group offices around the world. In 2001, HSBC also joined other HSBC Group members in providing customer access to "FX-All," a multi-bank global foreign exchange trading portal.

Corporate and Institutional Banking customers deal with the HSBC Group worldwide through a relationship manager. HSBC provides relationship management coverage to Canadian-based multinational clients and delivers services to other multinational clients of the HSBC Group. Our ability to leverage the HSBC Group's worldwide network in providing comprehensive corporate and investment banking services to sophisticated multinational clients is a significant competitive advantage.

A Wholesale Banking action plan was introduced during 2001. It was designed to implement a strategy of organizing around the needs of our larger corporate and commercial clients through alignment of Treasury, Corporate and Investment Banking to form a Wholesale Banking Unit. This plan combined the strengths of our corporate banking business with the corporate and commercial activities of HSBC Securities and the distribution capability of our treasury business. This has already had an impact with increased participation in many financings and increased our market share despite weak market conditions. Effective January 1, 2002, this new larger segment will be formally adopted for financial reporting purposes and will replace CIB as one of the reported business lines.

Selected Financial Information and Analysis. The following sets out consolidated financial information and other data for Corporate and Institutional Banking:

	Year ended December 31	
	2001	2000
	(in millions, except ratios)	
Net interest income	**$ 30**	$ 24
Provision for credit losses	**(4)**	(3)
Other income	**25**	17
Non-interest expenses	**(8)**	(7)
Income before the under noted:	**43**	31
Provision for income taxes	**(16)**	(13)
Non-controlling interest in income of subsidiaries	**(2)**	(1)
Net income	**$ 25**	$ 17
Average assets	**$ 2,447**	$ 2,193
Cost:income ratio	**14.5%**	17.1%

Corporate and Institutional Banking contributed $25 million (10.4%) to total net income for the year ended December 31, 2001, before unallocated corporate expenses. With $2.4 billion in average assets, Corporate and Institutional Banking represented 7.7% of total average assets for 2001.

Net interest income was higher in 2001 resulting from growth in loan facilities and from lower funding costs. Other income levels in 2001 benefited from higher credit fees generated from increased activity levels.

Treasury and Markets

The three principal activities of Treasury and Markets are client trading and facilitation, proprietary trading and balance sheet management.

Client Base. The HSBC Group's worldwide treasury and capital markets capabilities are used to enhance the opportunities to serve its clients. The HSBC Group's presence in these markets ranks among the largest in the world, serving governments, supra-nationals, multinational and domestic corporations and institutional and private investors.

Products and Services. Treasury and Markets provides the following products and services:

Client Trading and Facilitation	*Proprietary Trading*	*Balance Sheet Management*
Foreign exchange	Foreign exchange	Foreign exchange hedging
Derivatives	Fixed income securities	Interest rate hedging
Bankers' acceptances	Derivatives	Funding
Treasury bills	Equity trading	Investment/money market
Commercial paper	Client facilitation	Liquidity management
Medium term notes	Equity structured trading	
Equity sales and trading		
Equity research		

Management's Discussion and Analysis (continued)

Delivery Channels. The Domestic market is serviced through treasury operations in Toronto, Vancouver, Montreal and Calgary. Basic treasury products are also delivered through branches and through the HSBC Group's proprietary international payments and cash management platform, Hexagon. Institutional equity research, sales and trading services in Canadian securities are provided from offices in Toronto, Montreal, Calgary, Vancouver, New York, Boston and London.

Equity structured trading, which capitalizes on short-term arbitrage opportunities in North American equity markets, operates from offices in Toronto.

HSBC Bank Canada has joined other HSBC Group members in providing customer access to "FX-All", which is a multi-bank global electronic foreign exchange trading portal of which the HSBC Group is a founding member. FX-All provides a single point of access to participating foreign exchange providers – offering customers 24 hour online foreign currency trade execution and access to research.

Selected Financial Information and Analysis. The following sets out selected consolidated financial information and other data for Treasury and Markets:

	Year ended December 31	
	2001	2000
	(in millions, except ratios)	
Net interest income	**$ 37**	$ 30
Other income	**48**	82
Non-interest expenses	**(33)**	(59)
Income before the under noted:	**52**	53
Provision for income taxes	**(21)**	(23)
Non-controlling interest in income of subsidiaries	**(1)**	(1)
Net income	**$ 30**	$ 29
Average assets	**$ 6,734**	$ 5,942
Cost:income ratio	**38.8%**	52.7%

Treasury and Markets contributed $30 million (12.4%) to total net income for the year ended December 31, 2001, before unallocated corporate expenses. With $6.7 billion in average assets, Treasury and Markets represented 21.2 % of total average assets for 2001.

Net interest income for 2001 was higher than 2000 due to the growth in the balance sheet and from lower funding costs. Other income in 2001 continued to be adversely affected by weak equity markets during the year as trading income was lower. Non-interest expenses in 2001 were lower than 2000 due to lower performance-based compensation levels.

Consolidated Financial Statements

Statement of Management's Responsibility for Consolidated Financial Statements

The accompanying consolidated financial statements of HSBC Bank Canada have been prepared by, and are the responsibility of, the Bank's management. The presentation and information provided therein have been prepared in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada ("the Superintendent"). The financial statements necessarily include amounts based on informed judgements and estimates of the expected effects of current events and transactions with appropriate consideration to materiality.

In meeting its responsibility for the reliability of financial information, management relies on comprehensive internal accounting, operating and system controls. The Bank's overall controls include an organizational structure providing for effective segregation of responsibilities, delegation of authority and personal accountability; written communication of policies and procedures of corporate conduct throughout the Bank and careful selection and training of personnel; the regular updating and application of written accounting and administrative policies and procedures necessary to ensure adequate internal control over transactions, assets and records; as well as a continued program of extensive internal audit covering all aspects of the Bank's operations. These controls are designed to provide reasonable assurance that financial records are reliable for preparing financial statements and maintaining accountability for assets, that assets are safeguarded against unauthorized use or disposition and that the Bank is in compliance with all regulatory requirements including compliance with the Canada Deposit Insurance Corporation ("CDIC") Standards of Sound Business & Financial Practices. Annually, the Bank completes the Standards Assessment and Reporting Program ("SARP") which details the Bank's compliance with the CDIC standards.

The Superintendent, at least once a year, makes such examination and enquiry into the affairs of the Bank as he feels necessary to satisfy himself that the provisions of the Bank Act, having reference to the safety of the deposits and the Parent of the Bank, are being duly observed and that the Bank is in a sound financial position.

The Board of Directors oversees management's responsibilities for financial statements through the Audit Committee, which is composed solely of directors who are not officers or employees of the Bank. The Audit Committee meets four times per year. During each year it reviews the adequacy of internal controls over accounting and financial reporting systems and discusses with the internal and external auditors the overall scope, timing and specific plans for their respective audits. The Audit Committee reviews with management and the Shareholders' auditors the content and format of the Bank's financial statements. As part of this process it reviews the adoption of and changes in accounting principles and practices that have a material effect on the Bank's financial statements and key management estimates and judgements material to those statements. The Audit Committee also considers, for review by the Board and approval by the Parent, the engagement or re-appointment of the Shareholders' auditors. The annual SARP is approved by the Board.

The Shareholders' auditors, the Bank's Vice-President and Chief Auditor and the Superintendent have full and free access to the Audit Committee to discuss audit, financial reporting and related matters.

Martin J. G. Glynn
President and Chief Executive Officer

R. K. McGregor
Chief Financial Officer

January 21, 2002
Vancouver, Canada

Auditors' Report

To the Shareholders of HSBC Bank Canada

We have audited the consolidated balance sheets of HSBC Bank Canada as at December 31, 2001 and 2000 and the consolidated statements of income, changes in shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Bank as at December 31, 2001 and 2000 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada.

KPMG LLP

KPMG LLP
Chartered Accountants

Ernst + Young LLP

Ernst & Young LLP
Chartered Accountants

January 21, 2002
Vancouver, Canada

Consolidated Balance Sheets

As at December 31 *(in millions of dollars)*

	2001	2000
Assets		
Cash resources:		
Cash and deposits with Bank of Canada	**$ 466**	$ 375
Deposits with regulated financial institutions	**3,261**	1,997
	3,727	2,372
Securities: (note 2)		
Issued or guaranteed by Canada and provinces	**3,004**	2,990
Other securities	**623**	805
	3,627	3,795
Securities purchased under reverse repurchase agreements	**428**	436
Loans: (notes 3 & 4)		
Businesses and government	**11,575**	11,330
Residential mortgage	**8,377**	6,809
Consumer	**2,233**	1,899
Allowance for credit losses	**(315)**	(285)
	21,870	19,753
Other:		
Customers' liability under acceptances	**2,571**	2,134
Land, buildings and equipment (note 5)	**124**	118
Other assets (note 6)	**913**	830
	3,608	3,082
	$ 33,260	$ 29,438

See notes to consolidated financial statements

	2001	2000
Liabilities and Shareholders' Equity		
Deposits: (note 7)		
Regulated financial institutions	**$ 1,747**	$ 707
Individuals	**13,390**	12,116
Businesses and governments	**11,570**	10,688
	26,707	23,511
Other:		
Acceptances	**2,571**	2,134
Securities sold under repurchase agreements	**7**	15
Other liabilities (note 8)	**1,686**	1,720
Non-controlling interest in subsidiaries (note 9)	**230**	230
	4,494	4,099
Subordinated debentures (note 10)	**447**	422
Shareholders' equity:		
Capital stock (note 11)		
Preferred	**125**	125
Common	**935**	935
Contributed surplus	**165**	165
Retained earnings	**387**	181
	1,612	1,406
	$ 33,260	$ 29,438

Approved by the Board:

James H. Cleave
Chairman of the Board

Martin J. G. Glynn
President and Chief Executive Officer

Consolidated Statements of Income

For the years ended December 31 *(in millions of dollars except per share amounts)*

	2001	2000
Interest and dividend income:		
Loans	$ 1,448	$ 1,444
Securities	153	174
Deposits with regulated financial institutions	123	146
Total interest and dividend income	1,724	1,764
Interest expense:		
Deposits	938	1,068
Debentures	32	30
Total interest expense	970	1,098
Net interest income	754	666
Provision for credit losses (note 4)	92	39
Net interest income after provision for credit losses	662	627
Other income:		
Deposit and payment service charges	67	58
Credit fees	53	41
Capital market fees	98	162
Mutual fund and administration fees	51	48
Foreign exchange	49	47
Trade finance	24	22
Trading revenue	13	26
Securitization income	15	11
Other	49	47
	419	462
Net interest and other income	1,081	1,089
Non-interest expenses:		
Salaries and employee benefits	359	385
Premises and equipment expenses, including amortization	115	108
Other	230	249
Total non-interest expenses	704	742
Income before provision for income taxes and non-controlling interest in income of subsidiaries	377	347
Provision for income taxes (note 13)	147	155
Non-controlling interest in income of subsidiaries	16	8
Net income	$ 214	$ 184
Preferred share dividends	8	15
Net income applicable to common shares	$ 206	$ 169
Average number of common shares outstanding (000's)	456,168	325,305
Basic earnings per common share	$ 0.45	$ 0.52

See notes to consolidated financial statement

Consolidated Statements of Changes in Shareholders' Equity

For the years ended December 31 *(in millions of dollars)*

	2001	2000
Preferred shares: (note 11)		
Balance at beginning of year	**$ 125**	$ 270
Issued	**–**	125
Redeemed	**–**	(270)
Balance at end of year	**125**	125
Common shares: (note 11)		
Balance at beginning of year	**935**	75
Issued	**–**	860
Balance at end of year	**935**	935
Contributed surplus:		
Balance at beginning and end of year	**165**	165
Retained earnings:		
Balance at beginning of year	**181**	738
Net income	**214**	184
Gain on sale of subsidiary (note 22)	**–**	88
Preferred share dividends	**(8)**	(15)
Common share dividends	**–**	(810)
Share issuance costs	**–**	(4)
Balance at end of year	**387**	181
Total shareholders' equity	**$ 1,612**	$ 1,406

See notes to consolidated financial statements

Consolidated Statements of Cash Flows

For the years ended December 31 *(in millions of dollars)*

	2001	2000
Cash flows provided by (used in) operating activities:		
Net income	**$ 214**	$ 184
Adjustments to net income to determine net cash provided by (used in) operating activities:		
Amortization	**43**	40
Provision for credit losses (note 4)	**92**	39
Future income taxes (note 13)	**(7)**	24
Net accrued interest receivable and payable	**(6)**	12
Trading securities	**(198)**	(545)
Other, net	**(104)**	20
	34	(226)
Cash flows provided by (used in) financing activities:		
Deposits	**3,196**	2,275
Securities sold under repurchase agreements	**(8)**	(164)
Proceeds from preferred shares issued	**–**	125
Proceeds from common shares issued	**–**	860
Proceeds from debentures issued	**–**	25
Proceeds from asset trust securities issued	**–**	200
Redemption of preferred shares	**–**	(270)
Issuance costs	**–**	(4)
Dividends paid	**(8)**	(825)
	3,180	2,222
Cash flows provided by (used in) investing activities:		
Loans, excluding securitizations	**(2,273)**	(2,297)
Proceeds from loans securitized	**100**	606
Investment securities	**372**	(391)
Securities purchased under reverse repurchase agreements	**8**	(58)
Non-operating deposits with regulated financial institutions	**(555)**	169
Businesses acquired (note 21):	**(64)**	(124)
Less cash and cash equivalents at date of acquisition	**39**	270
Proceeds from sale of subsidiary (note 22):	**–**	110
Less cash and cash equivalents at date of sale	**–**	(6)
Land, buildings and equipment	**(41)**	(29)
	(2,414)	(1,750)
Increase in cash and cash equivalents	**800**	246
Cash and cash equivalents, beginning of year	**2,338**	2,092
Cash and cash equivalents, end of year	**$ 3,138**	$ 2,338
Represented by:		
Cash resources per consolidated balance sheet:	**$ 3,727**	$ 2,372
Less non-operating deposits with regulated financial institutions(1)	**(589)**	(34)
Cash and cash equivalents, end of year	**$ 3,138**	$ 2,338
Cash disbursements made for:		
Interest	**$ 1,031**	$ 1,047
Income taxes	**$ 191**	$ 133

(1) *Non-operating deposits are comprised primarily of cash which reprices after 90 days and cash restricted for recourse on securitization transactions.*

See notes to consolidated financial statements

Notes to Consolidated Financial Statements

December 31, 2001 and 2000 *(all tabular amounts are in millions of dollars)*

HSBC Bank Canada (the Bank) is a subsidiary of HSBC Holdings plc (the Parent). In these consolidated financial statements, Group means the Parent and its subsidiary companies.

1 Accounting policies

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles, including the accounting requirements of the Superintendent of Financial Institutions Canada. Certain prior period amounts have been reclassified to conform with the current year presentation. The significant accounting policies used in the preparation of these financial statements are summarized below.

a *Basis of consolidation*

The assets and liabilities and results of operations of the Bank and its subsidiaries are reported in the financial statements on a consolidated basis. All material intercompany transactions have been eliminated.

b *Use of estimates in preparation of consolidated financial statements*

The preparation of the consolidated financial statements of the Bank requires management to make estimates and assumptions based on information available as of the date of the financial statements. Therefore, actual results could differ from those estimates.

c *Deposits with regulated financial institutions*

Deposits with regulated financial institutions are recorded at cost. Interest income on interest earning deposits is recorded on an accrual basis.

d *Securities*

Investment account securities, where the Bank's intention is to hold the securities to maturity or until market conditions render alternative investments more attractive, are carried at cost or amortized cost. If the securities held for investment account experience a decline in value that is other than temporary, the carrying value is appropriately reduced. The amortization of premiums and discounts and adjustments to the carrying value of debt securities are included in interest income. Gains and losses on the disposal of securities are included in other income.

Trading account securities, which are purchased for resale over a short period of time, are carried at market value. Gains and losses on disposal or revaluation are included in other income.

Loan substitute securities are customer financings structured as after-tax investments to provide the borrower with an interest rate advantage over what would otherwise be applicable on a conventional loan. Such securities are accorded the accounting treatment applicable to loans.

e *Loans*

Loans are stated net of any unearned income, unamortized premiums or discounts and an appropriate allowance for credit losses.

Interest income is recorded on the accrual basis unless the loan is classified as an impaired loan. Loans are considered to be impaired whenever there is no longer reasonable assurance as to the ultimate collectibility of some portion of principal or interest. Loans where interest is due and has not been collected for a period of 90 days are automatically recognized as impaired, unless management determines there is no reasonable doubt as to the ultimate collectibility of principal and interest. Loans where interest is due and has not been collected for a period of 180 days are automatically classified as impaired.

Impaired loans are recorded at their estimated realizable amounts. This is determined by discounting the expected future cash flows at the effective interest rate inherent in the loans. When the amounts and timing of future cash flows cannot be estimated with reasonable reliability, they are measured at the fair value of any security underlying the loans, net of expected costs of realization. When a loan is classified as impaired, recognition of interest in accordance with the terms of the original loan agreement ceases. Subsequent payments (interest or principal) received on an impaired loan are recorded as a reduction of the recorded investment in the loan. Interest income is recognized only when all allowances for credit losses have been reversed.

Fees associated with lending activities are deferred and amortized over the term of the loans, and are included in income from loans in the consolidated statement of income.

Notes to Consolidated Financial Statements (continued)

1 Accounting policies *(continued)*

f *Direct finance leases*

Direct finance leases are included in commercial and other loans in the balance sheets. Initial direct costs of direct finance leases are expensed as incurred. The investment in the lease is defined as the minimum lease payments receivable, including the purchase option price, less unearned income.

g *Allowance for credit losses*

The Bank maintains an allowance for credit losses which is considered adequate to absorb all estimated credit related losses in its portfolio of both on and off-balance sheet items, including deposits with other regulated financial institutions, loan substitute securities, loans, acceptances, derivative instruments and other credit-related contingent liabilities, such as letters of credit and guarantees.

Assessing the adequacy of the allowance for credit losses is inherently subjective as it requires making estimates, including the amount and timing of expected future cash flows, that may be susceptible to significant change.

Specific allowances are recorded on a loan-by-loan basis, for those loans where management believes the ultimate collectibility of all or some portion of principal or interest is in doubt, to reduce the carrying value of an impaired asset to its estimated net realizable amount. The level of specific allowances are determined on an individual asset basis for all commercial loans and some personal loans while a formula approach is utilized for personal loans with similar characteristics. The determination of specific allowances is the responsibility of a dedicated unit that is independent of both the credit approval and credit line functions.

A number of methods are used in determining specific allowances including discounted value of future cash flows, observable market values or the fair values of the underlying security.

General allowances are allowances for losses which management estimates have occurred at the balance sheet date in the portfolio relating to loans within portfolios which give rise to credit risk but are not yet identified as non-performing loans and requiring specific provisions. In determining an appropriate level of general allowances, the Bank has adopted a methodology that incorporates the loan loss history as the basis for determining probability of default and loss given default rates for various credit portfolios that exhibit similar loan loss characteristics. These historic rates are further refined to allow for the stage of the credit cycle and the inherent difficulties in determining whether data collection captures a complete economic cycle. These loss ratios can then be applied to outstanding credit exposures to determine an appropriate level of allowance. Some credit portfolios do not readily lend themselves to this approach and therefore management have estimated an allowance level for these portfolios based on externally published default data or other underlying assumptions made as to the loan loss characteristics of these portfolios.

The provision for credit losses is charged to the consolidated statement of income and comprises the amounts written off during the year, net of recoveries on amounts written off in prior years, and changes in provisions.

h *Securities purchased and sold under repurchase agreements*

Where securities are sold subject to a commitment to repurchase them at a predetermined price, they remain on the balance sheet and a liability is recorded in respect of the consideration received.

Conversely, securities purchased under analogous commitments to resell are not recognized on the balance sheet and the consideration paid is recorded as a loan.

i *Land, buildings and equipment*

Land is carried at cost. Buildings, leasehold improvements and equipment are carried at cost, less accumulated amortization. Amortization is calculated using the straight-line method over the estimated useful life of the related asset as follows: buildings – 40 years, equipment – 3 to 5 years, and leasehold improvements – 10 to 15 years.

j *Goodwill and other intangible assets*

Goodwill represents the excess price paid for the acquisition of subsidiaries over the fair value of the net assets acquired and is recorded in other assets. Identifiable, reliably measured other intangible assets resulting from acquisition of subsidiaries are also recorded in other assets. Both goodwill and other intangible assets are amortized over the estimated period of benefit, not exceeding 15 years, except where a writedown is required to reflect impairment that is other than temporary.

1 Accounting policies *(continued)*

k *Acceptances*

The Bank's potential liability under acceptances is reported as a liability in the consolidated Balance Sheets. The Bank has equal and offsetting claims against its customers in the event of a call on these commitments, which are reported as an asset. Fees earned are reported in other income.

l *Income taxes*

The Bank follows the asset and liability method of accounting for income taxes. Under this method, future income tax assets and future income tax liabilities are determined based on temporary differences (differences between the tax basis and accounting basis of assets and liabilities) and are measured using the enacted or substantively enacted, tax rates expected to apply when the asset is realized or the liability is settled. A valuation allowance is recorded against any future tax asset if it is more likely than not that the asset will not be realized. Income tax expense or benefit is the sum of the provision for current income taxes and the difference between the opening and ending balances of the future income tax assets and liabilities.

m *Employee future benefits*

The Bank sponsors a number of pension plans covering substantially all employees. With one exception, these arrangements are defined benefit pension plans that provide a pension at retirement based on years of service with the Bank and average earnings prior to retirement. In addition, the Bank sponsors post-retirement non-pension arrangements that provide extended health, dental, life insurance and other benefits in retirement.

The costs of employee future benefits for defined benefits plans are determined using the projected unit credit method pro rata on service and using management's best estimate of expected investment performance, salary escalation and expected health care costs.

For purposes of determining the expected return on pension plan assets, those assets are valued at their fair market value.

The excess of net actuarial gains or losses over 10% of the greater of the accrued benefit obligation and the fair market value of plan assets is amortized over the average remaining service lifetimes of active employees covered under the plan in question. The weighted-average remaining service lifetime of the active employees under the pension plans is 15 years. The average remaining service period under the post-retirement non-pension arrangements is 20 years.

For the purposes of determining the financial position and the costs of employee future benefits, a measurement date of September 30 has been adopted.

n *Translation of foreign currencies*

Assets and liabilities in foreign currencies are translated into Canadian dollars at year-end spot exchange rates. Revenues and expenses in foreign currencies are translated into Canadian dollars at the rates in effect at the transaction date. Premiums and discounts on foreign currency forward contracts that hedge foreign currency assets and liabilities are amortized over the period to maturity as interest expense in the consolidated statement of income. Realized and unrealized gains and losses from foreign currency translation are included in other income in the consolidated statement of income.

o *Derivative instruments*

The Bank enters into interest rate, foreign exchange and equity derivative contracts in the normal course of business.

Trading derivatives are undertaken for proprietary trading, market making and to assist customers in managing their exposures. Trading derivatives are marked to market on a daily basis and the resulting gains and losses are recorded in other income. The unrealized portion of the gains and losses on trading derivatives is recorded in other assets or other liabilities as appropriate.

Asset/liability management derivatives are used to manage financial risks in the banking book such as movements in interest rates and foreign currency exchange rates. These derivatives are used to transfer these financial risks or to modify assets or liabilities or groups of similar on-balance sheet assets or liabilities. These contracts are accounted for on an accrual basis whereby the income or expense is recognized over the term of the agreement as an adjustment to interest revenue or expense. Accrued interest receivable and payable and deferred gains and losses are recorded in other assets or other liabilities as appropriate.

Notes to Consolidated Financial Statements (continued)

1 Accounting policies *(continued)*

p *Trust assets under administration*

Trust assets under administration are maintained separately from the Bank's assets and are not included in the consolidated balance sheets.

q *Loan securitizations*

The Bank periodically sells groups of loans to unrelated third parties. Effective July 1, 2001, the Bank adopted the Canadian Institute of Chartered Accountants' (CICA) accounting guideline for transfers of receivables. Transfers of loans occurring after June 30, 2001 are treated as sales provided that control over the transferred loans has been surrendered and consideration other than beneficial interests in the transferred loans has been received in exchange. If treated as sales, the loans are removed from the balance sheet and a gain or loss is recorded in other income immediately based on the carrying value of the loans transferred, allocated between the assets sold and their retained interests in proportion to their fair values at the date of transfer.

The fair values of loans sold, retained interests and recourse liabilities are determined using market values where appropriate or pricing models taking into account management's best estimates of key assumptions such as expected losses, prepayments and discount rates commensurate with the risks involved, or sales of similar assets. Where the Bank continues to service the loans sold, a servicing liability or asset is recognized and amortized over the servicing period as servicing fees.

For loans transferred prior to July 1, 2001 or transfers arising from commitments made prior to that date, transactions which transfer the risks and rewards of ownership and where there is reasonable assurance regarding the measurement of the consideration, are treated as sales and the loans are removed from the balance sheet. Gains on such transactions are deferred and included in other income when there is no recourse to the net proceeds. Losses are recognized in other income at the date of the sale.

Revenue earned by the Bank in respect of servicing the assets sold is reflected in other income as services are provided.

r *Future accounting changes*

Business combinations and goodwill and other intangible assets. The CICA issued two new related accounting standards on business combinations and accounting for goodwill and other intangible assets. The new standard on business combinations requires that all acquisitions initiated on or after July 1, 2001 be accounted for using the purchase method.

The standard for goodwill and other intangible assets is effective January 1, 2002. Under this new standard, goodwill will no longer be amortized but will be subject to a revised annual impairment test to identify any potential goodwill impairment. A goodwill impairment loss will be recognized if the fair value of the goodwill of a reporting unit is less than its carrying amount. The standard also requires that intangible assets with indefinite useful lives no longer be amortized, but be subject to an annual impairment test comparing fair values to carrying amounts.

An initial goodwill impairment review is required within six months of adoption. If any potential impairment is indicated, then it should be quantified based upon the fair value of the assets and liabilities of the reporting unit and, if necessary, recognized as a charge to opening retained earnings. The Bank does not anticipate any material impact on its financial statements in respect of either the initial adoption or the ongoing impact of this new standard.

The Bank will continue to amortize existing intangible assets other than goodwill over their estimated useful lives. These intangible assets will also be subject to an annual impairment test comparing carrying amounts to net recoverable amounts.

Stock-based compensation and other stock-based payments. The CICA has issued a new accounting standard for stock-based compensation and other stock-based payments which is effective January 1, 2002. The new standard requires the use of a fair-value-based method to account for certain stock-based compensation arrangements. There are some exemptions available for certain options granted by the Bank to employees that are not required to be accounted for using a fair-value-based method under the new standard. Accordingly, there will be no change to the Bank's existing accounting policies for these options. Pro-forma fair-value-based income and earnings per share disclosures will be required under the new standard. Consequently, there will be minimal impact on the Bank's Consolidated Statements of Income from the adoption of this new standard.

2 Securities

a *Carrying value*

	2001				
	Term to maturity				*Total carrying value*
	Within 1 year	*1-5 years*	*5-10 years*	*No specific maturity*	
Investment securities:					
Securities issued or guaranteed by:					
Canada	**$ 1,343**	**$ 637**	**$ 25**	**$ –**	**$ 2,005**
Provinces	**117**	**171**	**11**	**–**	**299**
	1,460	**808**	**36**	**–**	**2,304**
Others	**7**	**6**	**4**	**–**	**17**
Mutual funds	**–**	**–**	**–**	**27**	**27**
Equity securities	**14**	**11**	**6**	**5**	**36**
Total investment securities	**1,481**	**825**	**46**	**32**	**2,384**
Loan substitute securities	**40**	**50**	**–**	**–**	**90**
Trading securities	**664**	**55**	**85**	**349**	**1,153**
Total securities	**$ 2,185**	**$ 930**	**$ 131**	**$ 381**	**$ 3,627**

	2000				
	Term to maturity				*Total carrying value*
	Within 1 year	*1-5 years*	*5-10 years*	*No specific maturity*	
Investment securities:					
Securities issued or guaranteed by:					
Canada	$ 1,383	$ 880	$ 25	$ –	$ 2,288
Provinces	300	71	12	–	383
	1,683	951	37	–	2,671
Others	3	8	4	–	15
Mutual funds	–	–	–	25	25
Equity securities	13	20	6	5	44
Total investment securities	1,699	979	47	30	2,755
Loan substitute securities	–	85	–	–	85
Trading securities	676	57	–	222	955
Total securities	$ 2,375	$ 1,121	$ 47	$ 252	$ 3,795

Included in trading securities at December 31, 2001 are $700 million of securities issued or guaranteed by Canada or Provinces (2000 - $319 million).

The total carrying value of securities includes amounts denominated in U.S. dollars of $635 million (Canadian equivalent) (2000 - $746 million).

Notes to Consolidated Financial Statements (continued)

2 Securities *(continued)*

b *Unrealized gains and losses on investment securities*

	2001			
	Carrying value	*Gross unrealized gains*	*Gross unrealized losses*	*Estimated market value*
Securities issued or guaranteed by:				
Canada	**$ 2,005**	**$ 32**	**$ –**	**$ 2,037**
Provinces	**299**	**4**	**–**	**303**
	2,304	**36**	**–**	**2,340**
Others	**17**	**–**	**–**	**17**
Mutual funds	**27**	**–**	**(4)**	**23**
Equity securities	**36**	**–**	**(1)**	**35**
Total investment securities	**$ 2,384**	**$ 36**	**$ (5)**	**$ 2,415**

	2000			
	Carrying value	*Gross unrealized gains*	*Gross unrealized losses*	*Estimated market value*
Securities issued or guaranteed by:				
Canada	$ 2,288	$ 9	$ (7)	$ 2,290
Provinces	383	3	–	386
	2,671	12	(7)	2,676
Others	15	–	–	15
Mutual funds	25	–	(2)	23
Equity securities	44	–	–	44
Total investment securities	$ 2,755	$ 12	$ (9)	$ 2,758

3 Loans

a The Bank's loans outstanding, net of the allowance for credit losses, are as follows:

	2001	2000
Businesses and government:		
Real estate	**$ 3,504**	$ 3,406
Hotels and hospitality	**761**	718
Manufacturing	**1,783**	1,618
Trade	**2,922**	2,564
Services	**1,630**	2,137
Direct finance leases	**521**	443
Other	**454**	444
Total businesses and government	**11,575**	11,330
Residential mortgages	**8,377**	6,809
Consumer	**2,233**	1,899
Allowance for credit losses	**(315)**	(285)
Total	**$ 21,870**	$ 19,753

Total net loans includes amounts denominated in U.S. dollars of $1,707 million (Canadian equivalent) (2000 - $1,613 million) and other foreign currencies of $187 million (Canadian equivalent) (2000 - $113 million). Included in residential mortgages are $711 million of NHA insured mortgages (2000 - $414 million).

3 Loans *(continued)*

b The outstanding securitized loans sold to unrelated third parties and removed from the balance sheet are as follows:

	2001	2000
Residential mortgages		
Conventional	$ 390	$ 895
Mortgage-backed securities	530	691
Consumer loans	496	720
	$ 1,416	$ 2,306

Since July 1, 2001, (refer to Note 1), the Bank securitized residential mortgages of $100 million resulting in recognition of a net gain on sale, before income taxes, of $2 million. The Bank's retained interest, which consists of its rights to future cash flows, had a fair value of $4 million at the time of the transaction. The key assumptions used to measure fair value at the date of securitization were a prepayment rate of 14.4%, an excess spread of 1.4% and a discount rate of 6.3%. The mortgages securitized are government guaranteed and consequently credit losses are not expected.

4 Impaired loans and allowance for credit losses

a The Bank's total gross impaired loans and the related specific allowances are as follows:

	2001		
	Gross amount	*Specific allowances*	*Carrying amount*
Business and government			
Real estate	$ 82	$ 10	$ 72
Manufacturing	34	10	24
Trade	38	15	23
Services	12	6	6
Other	79	28	51
Consumer	13	10	3
Residential mortgages	24	1	23
Total	$ 282	$ 80	$ 202

	2000		
	Gross amount	*Specific allowances*	*Carrying amount*
Business and government			
Real estate	$ 41	$ 14	$ 27
Manufacturing	24	8	16
Trade	36	11	25
Services	14	7	7
Other	21	1	20
Consumer	14	9	5
Residential mortgages	24	1	23
Total	$ 174	$ 51	$ 123

Notes to Consolidated Financial Statements (continued)

4 Impaired loans and allowance for credit losses *(continued)*

b The Bank's allowance for credit losses is as follows:

	2001				
	Balance at beginning of the year	*Provision for credit losses*	*Write-offs*	*Recoveries and other*	*Balance at end of the year*
Specific allowances:					
Business and government:					
Real estate	**$ 14**	**$ 1**	**$ (5)**	**$ –**	**$ 10**
Manufacturing	**8**	**10**	**(8)**	**–**	**10**
Trade	**11**	**8**	**(6)**	**2**	**15**
Services	**7**	**3**	**(4)**	**–**	**6**
Other	**1**	**51**	**(32)**	**8**	**28**
Consumer	**9**	**9**	**(8)**	**–**	**10**
Residential mortgages	**1**	**2**	**(2)**	**–**	**1**
Total specific allowances	**51**	**84**	**(65)**	**10**	**80**
General allowance	**234**	**8**	**–**	**(7)**	**235**
Total	**$ 285**	**$ 92**	**$ (65)**	**$ 3**	**$ 315**

	2000				
	Balance at beginning of the year	*Provision for credit losses*	*Write-offs*	*Recoveries and other*	*Balance at end of the year*
Specific allowances:					
Business and government:					
Real estate	$ 9	$ 10	$ (5)	$ –	$ 14
Manufacturing	11	3	(6)	–	8
Trade	17	1	(7)	–	11
Services	12	9	(14)	–	7
Other	10	(2)	(7)	–	1
Consumer	12	6	(9)	–	9
Residential mortgages	1	1	(1)	–	1
Total specific allowances	72	28	(49)	–	51
General allowance	215	11	–	8	234
Total	$ 287	$ 39	$ (49)	$ 8	$ 285

5 Land, buildings and equipment

	Cost	*Accumulated amortization*	*Net book value* **2001**	*Net book value* 2000
Land and buildings	$ 24	$ 3	**$ 21**	$ 22
Furniture and equipment	116	82	**34**	30
Computer equipment	49	24	**25**	23
Leasehold improvements	87	43	**44**	43
Total	$ 276	$ 152	**$ 124**	$ 118

Amortization charged to income for the year ended December 31, 2001 amounted to $35 million (2000 - $34 million).

6 Other assets

	2001	2000
Accrued interest receivable	$ **90**	$ 146
Due from clients, dealers and clearing corporations	**251**	255
Market revaluation of trading derivatives (note 18)	**218**	127
Future income taxes, net (note 13)	**98**	95
Goodwill and other intangible assets, net	**43**	52
Accounts receivable and other	**213**	155
Total	$ **913**	$ 830

7 Deposits

	Regulated financial institutions	*Individuals*	*Businesses and governments*	*Total* **2001**
Demand	$ **102**	$ **–**	$ **1,035**	$ **1,137**
Notice	**–**	**2,728**	**3,735**	**6,463**
Fixed date	**1,645**	**10,662**	**6,800**	**19,107**
Total	$ **1,747**	$ **13,390**	$ **11,570**	$ **26,707**

	Regulated financial institutions	*Individuals*	*Businesses and governments*	*Total* 2000
Demand	$ 46	$ –	$ 856	$ 902
Notice	–	2,263	2,821	5,084
Fixed date	661	9,853	7,011	17,525
Total	$ 707	$ 12,116	$ 10,688	$ 23,511

Deposits denominated in U.S. dollars amount to $8,358 million (Canadian equivalent) (2000 - $6,684 million) and in other foreign currencies amount to $610 million (Canadian equivalent) (2000 - $587 million).

8 Other liabilities

	2001	2000
Accrued interest payable	$ **213**	$ 274
Mortgages sold with recourse	**131**	109
Payable to clients, dealers and clearing corporations	**456**	447
Market revaluation of trading derivatives (note 18)	**236**	136
Accounts payable and other	**650**	754
Total	$ **1,686**	$ 1,720

Notes to Consolidated Financial Statements (continued)

9 Non-controlling interest in subsidiaries

a *HSBC Canada Asset Trust*

HSBC Canada Asset Trust (the "Trust") was formed on May 26, 2000 as a closed-end trust, established under the laws of the Province of British Columbia by HSBC Trust Company (Canada), a subsidiary of the Bank, as trustee. The Trust's objective is to hold qualifying assets which will generate net income for distribution to holders of Trust Securities. The initial Trust assets are primarily undivided co-ownership interests in pools of Canada Mortgage and Housing Corporation ("CMHC") insured first mortgages originated by the Bank or its subsidiaries.

On June 28, 2000, the Trust issued 200,000 HSBC Canada Asset Trust Securities – Series 2010 ("HaTS") for gross proceeds of $200 million. Each of the HaTS were offered at $1,000 to provide an effective annual yield of 7.78% to December 31, 2010 and the six month bankers' acceptance rate plus 2.37% thereafter. Unless the Bank fails to declare dividends on its preferred shares, the Trust will make non-cumulative semi-annual cash distributions to the holders of each of the HaTS.

The Bank has covenanted that if the Trust fails to pay the indicated yield in full on the HaTS, the Bank will not declare dividends on any of its shares unless the Trust first pays the indicated yield.

The HaTS are not redeemable by the holders. Subject to regulatory approval, the Trust may redeem the HaTS on June 20, 2005 and on any distribution date thereafter.

b *HSBC Mortgage Corporation (Canada)*

HSBC Republic Holdings (Luxembourg) S.A. holds $30 million, a 100% interest, of class B perpetual preferred shares issued by HSBC Mortgage Corporation (Canada) ("HMC"), a wholly owned subsidiary of the Bank. No dividends were paid or payable on these perpetual preferred shares for the years ended December 31, 2001 and 2000. Dividends may be declared at the discretion of the directors of HMC.

10 Subordinated debentures

Debentures, which are unsecured and subordinated in right of payment to the claims of depositors and certain other creditors, comprise:

Interest rate (%)	*Year of maturity*	*Foreign currency amount*	**2001**	2000
Issued to Group companies				
7.09[(1)]	2094	US$85	$ **135**	$ 127
Issued to others				
8.50[(2)]	2002	EUR12	**17**	–
11.00[(2)]	2005		**60**	60
5.73[(3)]	2009		**60**	60
6.79[(4)]	2009		**50**	50
7.70[(5)]	2011		**60**	60
6.65[(6)]	2012		**25**	25
30 day bankers' acceptance rate plus 0.50%	2083		**40**	40
			312	295
Total			$ **447**	$ 422

(1) *The interest rate is fixed at 7.09% until July 2005 and thereafter the rate reprices every 5 years at the then 5 year U.S. Treasury rate plus 0.80%. Prior to July 2000, the interest rate was fixed at 6.84%.*

(2) *The interest rate is fixed until maturity.*

(3) *The interest rate is fixed at 5.73% until November 2004 and thereafter the rate reprices at the 90 day average bankers' acceptance rate plus 1.00%.*

(4) *The interest rate is fixed at 6.79% until December 2004 and thereafter the rate reprices at the 90 day average bankers' acceptance rate plus 1.00%*

(5) *The interest rate is fixed at 7.70% until February 2006 and thereafter the rate reprices at the 90 day average bankers' acceptance rate plus 1.00%.*

(6) *The interest rate is fixed at 6.65% until September 2007 and thereafter the rate reprices at the 90 day average bankers' acceptance rate plus 1.00%.*

Interest expense for the year ended December 31, 2001 relating to debentures issued to Group companies amounted to $9 million (2000 - $9 million).

11 Capital stock

Authorized:

Preferred – Unlimited number of Class 1 preferred shares in one or more series and unlimited number of Class 2 preferred shares in one or more series. The Board of Directors may from time to time divide any unissued Class 1 preferred shares into series and fix the number of shares in each series and the rights, privileges, restrictions and conditions.

Common – 993,677,000 common shares without par value.

Issued and fully paid:

	2001		2000	
	Number of shares	*Amount*	*Number of shares*	*Amount*
Preferred – Class 1, Series A[1]	**5,000,000**	**$ 125**	5,000,000	$ 125
Common[2]	**456,168,000**	**935**	456,168,000	935
		$ 1,060		$ 1,060

(1) *On June 28, 2000, the Bank issued 5,000,000 shares of non-voting, non-cumulative redeemable Class 1 Preferred Shares Series A for gross proceeds of $125 million. Each of the shares was offered at $25 per share to initially yield 6.25%, payable quarterly, as and when declared, until September 30, 2005. Subsequently, the dividend rate will be the greater of 6.00% or 95% of the average prime lending rate in Canada for the quarter immediately preceding the month in which the dividend is paid, as and when declared. During 2001, $8 million (2000 - $4 million) in dividends were declared and paid.*

The shares are not redeemable prior to September 30, 2005. Subject to regulatory approval on September 30, 2005, and on the last day of every successive period for five years and one day thereafter, the shares may be redeemed in whole by the Bank by the payment of cash equal to $25 per share plus all declared and unpaid dividends to the redemption date.

On September 30, 2005, and on the last day of every successive period for five years and one day thereafter, holders of shares will have the right to convert such shares into Preferred Shares Series B on a share-for-share basis, provided the Bank has not delivered a notice of redemption in respect of Preferred Shares Series A. The provisions of the Preferred Shares Series B are the same as those for Series A, except that the yield will be set to equal the 5 year Government of Canada bond rate 21 days preceding the date of conversion.

(2) *On August 23, 2000, the Bank issued 100,000,000 common shares for proceeds of $100 million. On November 17, 2000, the Bank issued 76,000,000 common shares for proceeds of $760 million.*

Dividend restrictions:

The Bank has covenanted that if the Trust fails to pay the indicated yield in full on the HaTS, the Bank will not declare dividends on any of its shares unless the Trust first pays the indicated yield.

Notes to Consolidated Financial Statements (continued)

12 Employee future benefits

The Bank sponsors a number of pension arrangements covering its employees. With one exception, these are defined benefit plans. In addition, the Bank sponsors post-retirement non-pension arrangements covering its employees.

Information about the defined benefit plans, in aggregate, as at December 31 (using a measurement date of September 30 – see note 1) is as follows:

	Pension benefits		*Other benefits*	
	2001	2000	**2001**	2000
Reconciliation of accrued benefit obligation				
Accrued benefit obligation, beginning of year	**$ 129**	$ 114	**$ 42**	$ –
Adoption of new standard	**–**	4	**–**	38
Service cost	**7**	6	**3**	3
Interest cost	**10**	9	**3**	3
Benefits paid	**(9)**	(8)	**(1)**	(1)
Actuarial loss (gain)	**14**	3	**2**	(1)
Employee contributions	**1**	1	**–**	–
Accrued benefit obligation, end of year	**$ 152**	$ 129	**$ 49**	$ 42
Reconciliation of fair value of plan assets				
Fair value of plan assets, beginning of year	**$ 189**	$ 175	**$ –**	$ –
Return on plan assets	**(33)**	16	**–**	–
Employer contributions	**6**	5	**1**	1
Employee contributions	**1**	1	**–**	–
Benefits paid	**(9)**	(8)	**(1)**	(1)
Fair value of plan assets, end of year	**$ 154**	$ 189	**$ –**	$ –
Funded status				
Funded status – plan surplus (deficit)	**$ 2**	$ 60	**$ (49)**	$ (42)
Employer contributions after measurement date	**2**	2	**–**	–
Unamortized net actuarial loss (gain)	**62**	–	**1**	(1)
Unamortized transitional (asset) obligation	**(53)**	(57)	**34**	36
Accrued benefit asset (liability)	**13**	5	**(14)**	(7)
Valuation allowance	**(5)**	–	**–**	–
Accrued benefit asset (liability), net of valuation allowance	**$ 8**	$ 5	**$ (14)**	$ (7)

Included in the above accrued benefit obligations and fair value of pension plan assets at year-end are the following amounts in respect of pension plans that are not fully funded:

	2001	2000
Accrued benefit obligation	**$ 71**	$ 15
Fair value of plan assets	**41**	–
Funded status – deficit	**$ 30**	$ 15

12 Employee future benefits *(continued)*

The following table shows the components of net periodic defined benefit cost:

	Pension benefits				*Other benefits*			
		2001		2000		**2001**		2000
Service cost	**$**	**7**	$	6	**$**	**3**	$	3
Interest costs		**10**		9		**3**		3
Expected return on plan assets		**(15)**		(14)		**–**		-
Amortization of transitional obligation (asset)		**(4)**		(1)		**2**		2
Increase in valuation allowance		**5**		–		**–**		–
Net benefit plan expense	**$**	**3**	$	–	**$**	**8**	$	8

The expense for the Bank's defined contribution pension plan was $2 million (2000 - $2 million).

The significant actuarial assumptions adopted in measuring the Bank's accrued benefit obligations are as follows (weighted-average assumptions as of December 31):

	Pension benefits		*Other benefits*	
	2001	2000	**2001**	2000
Discount rate	**7.25%**	7.25%	**7.25%**	7.50%
Expected long-term rate of return on plan assets	**8.0%**	8.0%	**–**	
Rate of compensation increase	**4.0%**	4.0%	**4.0%**	4.0%

For measurement purposes, a 5.9% health care cost trend rate was assumed grading down to 3.9% by 2004 and assumed to remain level thereafter.

13 Income taxes

a Provisions for income taxes included in the consolidated statements of income are:

		2001		2000
Current income taxes:				
Federal	**$**	**100**	$	86
Provincial		**54**		45
		154		131
Future income taxes:				
Federal		**(4)**		16
Provincial		**(3)**		8
		(7)		24
Total income taxes	**$**	**147**	$	155

Notes to Consolidated Financial Statements (continued)

13 Income taxes *(continued)*

b The provisions for income taxes shown in the consolidated statements of income are less than that obtained by applying statutory tax rates to the net income before provision for income taxes, less non-controlling interest in income of subsidiaries, for the following reasons:

	2001	2000
Combined federal and provincial income tax rate	**43.2%**	45.2%
Adjustments resulting from:		
Adjustment for tax exempt income related to preferred shares, common shares, and income debentures	**(2.4)**	(2.9)
Utilization of tax losses carried forward and other deductions	**(3.9)**	(10.3)
Substantively enacted tax rate changes	**1.8**	5.0
Additional financial institution taxes	**0.5**	1.4
Other, net	**1.5**	7.3
Effective tax rate	**40.7%**	45.7%

c The net future income tax asset reported in other assets is comprised as follows:

	2001	2000
Future income tax assets:		
Allowance for credit losses	**$ 81**	$ 85
Other available deductions	**28**	28
Non-capital losses	**15**	26
Other	**9**	5
	133	144
Valuation allowance	**–**	(3)
	133	141
Future income tax liabilities:		
Leases	**(19)**	(23)
Intangible assets	**(13)**	(17)
Other	**(3)**	(6)
	(35)	(46)
Net future income tax asset	**$ 98**	$ 95

14 Long-term lease commitments

Future minimum commitments under long-term leases of premises are as follows:

2002	$ 32
2003	29
2004	27
2005	23
2006	19
2007 and thereafter	60
	$ 190

The total rental expense charged in respect of premises for the year ended December 31, 2001 was $42 million (2000 - $40 million).

15 Guarantees and letters of credit

The Bank issues guarantees and letters of credit to meet credit requirements of certain customers. The amounts are not included in the consolidated balance sheets and are as follows:

	2001	2000
Guarantees	**$ 1,169**	$ 970
Letters of credit	**469**	408
	$ 1,638	$ 1,378

In the event of a call on the above commitments, the Bank has recourse against those customers who have requested the guarantees or letters of credit.

16 Contingencies

A Bank subsidiary is subject to threatened actions relating to its responsibilities as a distributor, escrow agent and custodian. Based upon information presently available, counsel for the Bank are not in a position to express an opinion as to the likely outcome. Accordingly, no provisions have been recorded in the consolidated financial statements relating to these matters.

The Bank and its subsidiaries are subject to a number of other legal proceedings arising in the normal course of their businesses. Management does not expect the outcome of any of these other proceedings, in aggregate, to have a material effect on the consolidated financial position or results of the Bank's operations.

The Bank is subject to limited recourse for potential credit losses on all assets securitized and potential shortfall of yield on certain of the assets securitized. As at December 31, 2001, the total recourse against the Bank under securitization transactions was $23 million (2000 - $29 million).

17 Fair value of financial instruments

The amounts below represent the fair values of the Bank's on-balance sheet financial instruments at December 31. Fair value is the estimated amount of the consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act and is best evidenced by a quoted market price, if one exists.

Many of the Bank's financial instruments lack an available trading market. Therefore, these instruments have been valued using present value or other valuation techniques and may not necessarily be indicative of the amounts realizable in an immediate settlement of the instruments. In addition, the calculation of estimated fair value is based on market conditions at a specific point in time and may not be reflective of future fair values.

Changes in interest rates are the main cause of changes in the fair value of the Bank's financial instruments. The majority of the Bank's financial instruments are carried at historical cost and are not adjusted to reflect increases or decreases in fair value due to market fluctuations, including those due to interest rate changes. For those financial instruments held for trading purposes, the carrying value is adjusted daily to reflect the fair value.

Notes to Consolidated Financial Statements (continued)

17 Fair value of financial instruments *(continued)*

	2001						2000					
	Book value		*Fair value*		*Fair value over (under) book value*		*Book value*		*Fair value*		*Fair value over (under) book value*	
Assets												
Cash resources	$	**3,727**	$	**3,727**	$	**–**	$	2,372	$	2,372	$	–
Securities (Note 2)		**3,627**		**3,658**		**31**		3,795		3,798		3
Securities purchased under reverse repurchase agreements		**428**		**428**		**–**		436		436		–
Loans		**21,870**		**22,134**		**264**		19,753		19,783		30
Acceptances		**2,571**		**2,571**		**–**		2,134		2,134		–
Other assets		**913**		**913**		**–**		830		830		–
Liabilities												
Deposits	$	**26,707**	$	**26,839**	$	**132**	$	23,511	$	23,556	$	45
Acceptances		**2,571**		**2,571**		**–**		2,134		2,134		–
Securities sold under repurchase agreements		**7**		**7**		**–**		15		15		–
Other liabilities		**1,686**		**1,686**		**–**		1,720		1,720		–
Subordinated debt		**447**		**477**		**30**		422		436		14

The determination of fair values of financial instruments for which there are no quoted market values requires that a number of assumptions are made for which there exists a significant degree of subjectivity. The following methods and assumptions were used to estimate the fair value of these financial instruments:

- Cash resources, acceptances, other assets, securities purchased under reverse repurchase agreements, securities sold under repurchase agreements and other liabilities, due to their short term nature, are assumed to approximate their carrying values.
- Investment securities are assumed to be equal to the estimated market value of securities provided in Note 2. These values are based on quoted market prices where available. If quoted market prices are not available, fair values are estimated using quoted market prices of similar securities or other valuation techniques. Trading securities have carrying values which are equal to their estimated market value.
- Floating rate and consumer loans are assumed to be equal to their book value. The fair value of commercial and residential mortgage loans with fixed terms are estimated using a discounted cash flow calculation at current rates for loans with similar terms and credit risks.
- Demand and floating rate deposits are assumed to be equal to their carrying value. The fair value of fixed rate deposits is estimated using a discounted cash flow calculation at market rates.
- Subordinated debt is determined by reference to current market prices for debt with similar terms and risks.

18 Derivative instruments

In the ordinary course of business, the Bank enters into various derivative contracts such as foreign exchange contracts, interest rate swaps, forward rate agreements and financial futures contracts whose notional principal is not included in the consolidated balance sheets.

Derivatives are contracts whose value is derived from an underlying asset or an underlying reference rate or index such as interest or foreign exchange rates. The Bank uses derivatives for both trading and asset/liability management purposes.

Trading related activity includes transactions undertaken on behalf of the Bank and its customers ("Trading"). Asset/liability management derivatives are used by the Bank to manage its exposures to interest rate and foreign currency fluctuations and where appropriate the Bank may use customer related trading transactions as part of its asset/liability management ("ALM") program.

The Bank strictly adheres to its formalized risk management policies and procedures. Risk limits are determined for each portfolio of derivative instruments based on product, currency, interest rate repricing and market volatility. All limits are monitored on a daily basis.

Derivative instruments are subject to both market risk and credit risk. Market risk is the risk that the fair value of derivatives will fluctuate due to changes in interest, foreign exchange rates, and equity markets. Market risk is managed on a consolidated Bank basis.

Credit risk for derivative instruments is not equal to the notional amount of the principal as it is with assets recorded on the balance sheets. The credit risk for derivatives is principally the replacement cost of any contract with a positive market value plus an estimate for future fluctuation risk. Credit risk for derivatives is managed using the Bank's risk management policies.

a An analysis of the Bank's derivative portfolio and related credit exposure at December 31 is as follows:

	2001				2000			
	Notional amount	*Current replacement cost*	*Credit equivalent amount*	*Risk weighted balance*	*Notional amount*	*Current replacement cost*	*Credit equivalent amount*	*Risk weighted balance*
Interest rate contracts								
Forward rate agreements	**$ 1,529**	**$ 2**	**$ 2**	**$ 1**	$ 90	$ –	$ –	$ –
Futures – exchange traded	**1,101**	**–**	**–**	**–**	1,077	–	–	–
Swaps	**6,982**	**177**	**179**	**50**	8,411	54	80	23
Caps	**137**	**–**	**1**	**–**	54	–	–	–
	9,749	**179**	**182**	**51**	9,632	54	80	23
Foreign exchange contracts								
Spot contracts	**290**	**–**	**–**	**–**	519	1	1	–
Forward contracts	**14,703**	**230**	**456**	**130**	13,736	130	324	85
Currency swaps and options	**2,670**	**2**	**18**	**7**	311	1	13	4
	17,663	**232**	**474**	**137**	14,566	132	338	89
Equity contracts	**275**	**–**	**12**	**2**	152	–	11	5
Total	**$ 27,687**	**$ 411**	**$ 668**	**$ 190**	$ 24,350	$ 186	$ 429	$ 117
Impact of master netting agreements		**(50)**	**(92)**	**(18)**		(23)	(27)	(8)
		$ 361	**$ 576**	**$ 172**		$ 163	$ 402	$ 109

Notes to Consolidated Financial Statements (continued)

18 Derivative instruments *(continued)*

Notional amounts are the contract amounts used to calculate the cash flows to be exchanged. They are a common measure of volume of outstanding transactions, but do not represent credit or market risk exposure.

Current replacement cost represents the estimated cost of replacing, at current market rates, all contracts with a positive value.

Credit equivalent amount is the current replacement cost plus an amount for future credit exposure associated with the potential for future changes in currency and interest rates. The future credit exposure is calculated using a formula prescribed by the Superintendent in its capital adequacy guidelines.

Risk-weighted balance represents the amount based upon which the regulatory capital required to support the Bank's derivative activities is calculated. It is derived from risk weighting the credit equivalent amounts according to the creditworthiness of the counter parties using factors prescribed by the Superintendent in its capital adequacy guidelines.

b The following tables summarize the notional amounts by remaining term to maturity of the Bank's derivative portfolio at December 31, segregating derivative instruments between those entered into by the Bank for its customer and proprietary trading activities and those used to manage the risk associated with changes in interest and foreign exchange rates as part of the Bank's ALM program.

	2001								
	Trading				*ALM*				
	Under 1 year	*1 - 5 years*	*Over 5 years*	*Total trading*	*Under 1 year*	*1 - 5 years*	*Over 5 years*	*Total ALM*	*Total*
Interest rate contracts									
Forward rate agreements	$ 1,529	$ –	$ –	$ 1,529	$ –	$ –	$ –	$ –	$ 1,529
Futures – exchange traded	982	119	–	1,101	–	–	–	–	1,101
Swaps	1,680	1,737	318	3,735	1,027	1,831	389	3,247	6,982
Caps	80	57	–	137	–	–	–	–	137
	4,271	1,913	318	6,502	1,027	1,831	389	3,247	9,749
Foreign exchange contracts									
Spot contracts	290	–	–	290	–	–	–	–	290
Forward contracts	8,057	2,107	–	10,164	4,530	9	–	4,539	14,703
Currency swaps and options	2,620	8	–	2,628	24	7	11	42	2,670
	10,967	2,115	–	13,082	4,554	16	11	4,581	17,663
Equity contracts	275	–	–	275	–	–	–	–	275
Total	$ 15,513	$ 4,028	$ 318	$ 19,859	$ 5,581	$ 1,847	$ 400	$ 7,828	$ 27,687

18 Derivative instruments *(continued)*

	2000								
	Trading				*ALM*				
	Under 1 year	*1 - 5 years*	*Over 5 years*	*Total trading*	*Under 1 year*	*1 - 5 years*	*Over 5 years*	*Total ALM*	*Total*
Interest rate contracts									
Forward rate agreements	$ 90	$ –	$ –	$ 90	$ –	$ –	$ –	$ –	$ 90
Futures – exchange traded	965	112	–	1,077	–	–	–	–	1,077
Swaps	1,419	1,763	69	3,251	2,586	2,274	300	5,160	8,411
Caps	–	54	–	54	–	–	–	–	54
	2,474	1,929	69	4,472	2,586	2,274	300	5,160	9,632
Foreign exchange contracts									
Spot contracts	519	–	–	519	–	–	–	–	519
Forward contracts	8,774	1,344	–	10,118	3,408	210	–	3,618	13,736
Currency swaps and options	100	183	–	283	–	17	11	28	311
	9,393	1,527	–	10,920	3,408	227	11	3,646	14,566
Equity contracts	152	–	–	152	–	–	–	–	152
Total	$ 12,019	$ 3,456	$ 69	$ 15,544	$ 5,994	$ 2,501	$ 311	$ 8,806	$ 24,350

c The following tables summarize the fair values, as represented by the sum of the net unrealized gains and losses, accrued interest receivable and payable and premiums paid or received, of the Bank's derivative portfolio at December 31 segregating derivative instruments between trading and ALM and between those that are in a favourable or receivable position from those in an unfavourable or payable position.

Trading derivatives are marked to market on a daily basis and the net position for the trading portfolio shown in the table below has already been recognized in the financial statements. ALM interest rate derivatives are accounted for on the accrual basis and the net income or expense is recognized over the life of the derivative contract. Foreign exchange derivatives used for ALM purposes are accounted for on an accrual basis as are the underlying assets and liabilities hedged. The ALM portfolio is used to manage the Bank's exposure to changes in interest and foreign currency rates. Consequently, the net favourable or unfavourable position in the ALM portfolio shown in the table below is approximately offset by changes in the values in the underlying hedged assets and liabilities.

Fair values of derivative instruments are determined using quoted market prices.

Notes to Consolidated Financial Statements (continued)

18 Derivative instruments *(continued)*

2001

	Trading			ALM			
	Favourable position	*(Unfavourable) position*	*Net position*	*Favourable position*	*(Unfavourable) position*	*Net position*	*Total net*
Interest rate contracts							
Forward rate agreements	$ 2	$ (2)	$ –	$ –	$ –	$ –	$ –
Futures	–	–	–	–	–	–	–
Swaps	66	(64)	2	111	(18)	93	95
Caps	–	–	–	–	–	–	–
	68	(66)	2	111	(18)	93	95
Foreign exchange contracts							
Spot contracts	–	–	–	–	–	–	–
Forward contracts	149	(149)	–	81	(4)	77	77
Currency swaps and options	1	(15)	(14)	1	(2)	(1)	(15)
	150	(164)	(14)	82	(6)	76	62
Equity contracts	–	(6)	(6)	–	–	–	(6)
Total	$ 218	$ (236)	$ (18)	$ 193	$ (24)	$ 169	$ 151

2000

	Trading			ALM			
	Favourable position	*(Unfavourable) position*	*Net position*	*Favourable position*	*(Unfavourable) position*	*Net position*	*Total net*
Interest rate contracts							
Forward rate agreements	$ –	$ –	$ –	$ –	$ –	$ –	$ –
Futures	–	–	–	–	–	–	–
Swaps	19	(17)	2	35	(10)	25	27
Caps	–	–	–	–	–	–	–
	19	(17)	2	35	(10)	25	27
Foreign exchange contracts							
Spot contracts	1	(1)	–	–	–	–	–
Forward contracts	106	(114)	(8)	24	(41)	(17)	(25)
Currency swaps and options	1	(3)	(2)	–	(2)	(2)	(4)
	108	(118)	(10)	24	(43)	(19)	(29)
Equity contracts	–	(1)	(1)	–	–	–	(1)
Total	$ 127	$ (136)	$ (9)	$ 59	$ (53)	$ 6	$ (3)

19 Interest rate sensitivity position

The following table provides an analysis of the Bank's interest rate sensitivity position at December 31 based on contractual repricing dates of assets and liabilities:

	2001									
	Within 3 months	*3 to 6 months*	*6 to 12 months*	*Effective interest rate (%)*	*1 to 5 years*	*Effective interest rate (%)*	*Greater than 5 years*	*Effective interest rate (%)*	*Non-interest sensitive*	*Total*
Cash resources	$ 2,954	$ 239	$ 239	2.5	$ 5	6.3	$ –	–	$ 290	$ 3,727
Securities	1,551	528	305	3.5	823	5.2	39	4.6	381	3,627
Securities purchased under reverse repurchase agreements	428	–	–	2.0	–	–	–	–	–	428
Loans	12,102	1,290	2,123	4.7	6,206	6.6	182	7.4	(33)	21,870
Other assets	–	–	–	–	–	–	–	–	3,608	3,608
Total assets	17,035	2,057	2,667	–	7,034	–	221	–	4,246	33,260
Deposits	15,441	2,917	4,087	2.1	902	5.5	9	5.6	3,351	26,707
Securities sold under repurchase agreements	7	–	–	2.0	–	–	–	–	–	7
Other liabilities	–	–	–	–	–	–	–	–	4,257	4,257
Non-controlling interest in subsidiaries	–	–	–	–	–	–	200	7.8	30	230
Subordinated debt	40	–	18	4.6	364	7.6	25	7.6	–	447
Shareholders' equity	–	–	–	–	125	6.3	–	–	1,487	1,612
Total liabilities & shareholders' equity	15,488	2,917	4,105	–	1,391	–	234	–	9,125	33,260
On balance sheet gap	1,547	(860)	(1,438)	–	5,643	–	(13)	–	(4,879)	–
Off balance sheet positions	(689)	(576)	121	–	934	–	210	–	–	–
Total interest rate gap	$ 858	$(1,436)	$(1,317)	–	$ 6,577	–	$ 197	–	$(4,879)	$ –

Notes to Consolidated Financial Statements (continued)

19 Interest rate sensitivity position *(continued)*

	2000									
	Within 3 months	*3 to 6 months*	*6 to 12 months*	*Effective interest rate (%)*	*1 to 5 years*	*Effective interest rate (%)*	*Greater than 5 years*	*Effective interest rate (%)*	*Non-interest sensitive*	*Total*
Cash resources	$ 2,098	$ –	$ –	6.4	$ 6	6.7	$ –	–	$ 268	$ 2,372
Securities	1,778	330	365	6.4	981	6.2	39	5.9	302	3,795
Securities purchased under reverse repurchase agreements	436	–	–	–	–	–	–	–	–	436
Loans	11,295	1,309	1,792	7.6	5,298	7.0	170	7.8	(111)	19,753
Other assets	–	–	–	–	–	–	–	–	3,082	3,082
Total assets	15,607	1,639	2,157	–	6,285	–	209	–	3,541	29,438
Deposits	13,928	2,669	3,148	5.1	1,094	6.1	13	7.3	2,659	23,511
Securities sold under repurchase agreements	15	–	–	–	–	–	–	–	–	15
Other liabilities	–	–	–	–	–	–	–	–	3,854	3,854
Non-controlling interest in subsidiaries	–	–	–	–	–	–	200	7.8	30	230
Subordinated debt	40	–	–	–	297	7.6	85	7.4	–	422
Shareholders' equity	–	–	–	–	125	6.3	–	–	1,281	1,406
Total liabilities & shareholders' equity	13,983	2,669	3,148	–	1,516	–	298	–	7,824	29,438
On balance sheet gap	1,624	(1,030)	(991)	–	4,769	–	(89)	–	(4,283)	–
Off balance sheet positions	(709)	(470)	(103)	–	1,058	–	224	–	–	–
Total interest rate gap	$ 915	$(1,500)	$(1,094)	–	$ 5,827	–	$ 135	–	$(4,283)	$ –

An immediate and sustained parallel increase in interest rates of 1% across all currencies and maturities would reduce net interest income by $25 million (2000 - $15 million) over the next twelve months assuming no additional hedging is undertaken.

In managing interest rate risk, the Bank relies primarily upon its contractual interest rate sensitivity position adjusted for certain assumptions regarding customer behavioral preferences, which are based upon historical trends. Adjustments made include assumptions relating to early repayment of consumer loans and residential mortgages and customer preferences for demand, notice and redeemable deposits. Based upon these adjustments, it is estimated that an immediate and sustained parallel increase in interest rates of 1% across all currencies and maturities would decrease net interest income by $13 million (2000 - $6 million) over the next twelve months assuming no additional hedging is undertaken.

20 Segmented information

a *Business Lines:*

The Bank's reportable segments are strategic business lines that offer different products and services. The Bank primarily measures the performance of each business line based on the net income of the business line. A description of each segment is as follows:

Personal financial services provides a range of personal financial services to individuals through the Bank's branches and subsidiary offices, ABMs and other electronic delivery channels such as Internet, PC and telephone. Services included in this segment include: retail and private banking; PC and telephone banking; card services; full service brokerage; asset management, including retirement products; direct sale home and automotive insurance; and trust and advisory services.

Commercial financial services provide credit, loan syndication, trade finance, foreign exchange and commercial and investment banking activities to the Bank's mid-market commercial clients. The commercial banking business line also includes institutional fund management services.

Corporate and institutional banking provides full service commercial and investment banking products and services to the Group's largest multinational corporate clients.

Treasury and markets encompasses results of activities from the Bank's treasury department and trading activities from the Bank's full service brokerage subsidiary. Treasury and Markets also includes trading in foreign exchange, fixed income securities, equity and derivative products.

Other includes the effect of consolidation adjustments and unallocated revenues and expenses.

The accounting policies of the segments are generally consistent with those followed in the preparation of the consolidated financial statements as disclosed in Note 1.

	Year ended December 31, 2001					
	Personal financial services	*Commercial financial services*	*Corporate and institutional banking*	*Treasury and markets*	*Other*	*Total*
Net interest income	$ **326**	$ **361**	$ **30**	$ **37**	$ **–**	$ **754**
Provision for credit losses	**(20)**	**(68)**	**(4)**	**–**	**–**	**(92)**
Other income	**182**	**164**	**25**	**48**	**–**	**419**
Non-interest expenses	**(341)**	**(277)**	**(8)**	**(33)**	**(45)**	**(704)**
Income before the under noted:	**147**	**180**	**43**	**52**	**(45)**	**377**
Provision for income taxes	**(58)**	**(70)**	**(16)**	**(21)**	**18**	**(147)**
Non-controlling interest in income of subsidiaries	**(5)**	**(8)**	**(2)**	**(1)**	**–**	**(16)**
Net income	$ **84**	$ **102**	$ **25**	$ **30**	$ **(27)**	$ **214**
Average assets	$ **9,981**	$ **12,685**	$ **2,447**	$ **6,734**	$ **–**	$ **31,847**

Notes to Consolidated Financial Statements (continued)

20 Segmented information *(continued)*

	Year ended December 31, 2000					
	Personal financial services	*Commercial financial services*	*Corporate and institutional banking*	*Treasury and markets*	*Other*	*Total*
Net interest income	$ 300	$ 312	$ 24	$ 30	$ –	$ 666
Provision for credit losses	(11)	(25)	(3)	–	–	(39)
Other income	211	152	17	82	–	462
Non-interest expenses	(372)	(263)	(7)	(59)	(41)	(742)
Income before the under noted:	128	176	31	53	(41)	347
Provision for income taxes	(56)	(76)	(13)	(23)	13	(155)
Non-controlling interest in income of subsidiaries	(2)	(4)	(1)	(1)	–	(8)
Net income	$ 70	$ 96	$ 17	$ 29	$ (28)	$ 184
Average assets	$ 9,287	$ 11,061	$ 2,193	$ 5,942	$ –	$ 28,483

b *Geographic*:

	2001			
	Assets		*Liabilities*	
	Amount	*Percent*	*Amount*	*Percent*
Canada	**$ 30,184**	**90.8**	**$ 25,620**	**81.5**
United States	**2,136**	**6.4**	**1,810**	**5.8**
Hong Kong SAR	**127**	**0.4**	**2,156**	**6.9**
Other	**813**	**2.4**	**1,832**	**5.8**
Total	**$ 33,260**	**100.0**	**$ 31,418**	**100.0**

	2000			
	Assets		*Liabilities*	
	Amount	*Percent*	*Amount*	*Percent*
Canada	$ 27,484	93.3	$ 23,178	83.4
United States	1,767	6.0	1,018	3.7
Hong Kong SAR	53	0.2	2,063	7.4
Other	134	0.5	1,543	5.5
Total	$ 29,438	100.0	$ 27,802	100.0

Assets are allocated on the basis of the location of ultimate risk. Liabilities are allocated on the basis of the residence status of the bearer of the deposit, acceptances or other liability.

21 Business acquisitions and long-term investments

a *2001 acquisitions*

Effective March 19, 2001, the Bank acquired all the voting shares of CCF Canada ("CCFC") from a Group company and all of the non-voting Special Shares from Crédit Lyonnais Global Banking at carrying amounts. Prior to the acquisition by the Bank, CCFC was formed by the amalgamation of CCFC and Crédit Lyonnais Canada and continued under the name of CCFC. On April 1, 2001, CCFC was amalgamated with the Bank.

21 Business acquisitions and long-term investments *(continued)*

The acquisition was accounted for as an exchange of ownership interests under common control using the carrying amounts of the net assets acquired which consisted of:

Tangible assets	**$**	**96**
Liabilities		**(32)**
Net assets acquired for cash consideration	**$**	**64**

b *2000 acquisitions*

Effective April 1, 2000, the Bank acquired all of the voting shares of Republic National Bank of New York (Canada) ("Republic Canada"). Republic Canada was acquired from a Group company at carrying amounts. The carrying amounts were supported using an independent third party valuation. Immediately subsequent to the acquisition, Republic Canada was amalgamated with the Bank.

The acquisition was accounted for as an exchange of ownership interests under common control using the carrying amounts of the net assets acquired which consisted of:

Tangible assets	$	1,256
Intangible assets		51
Liabilities		(1,183)
Net assets acquired for cash consideration	$	124

22 Related party transactions

On November 29, 2000 the Bank sold to a Group company, its 100% interest in HSBC InvestDirect (Canada) Inc. ("HIDC") for cash consideration of $110 million. The transfer price was determined using an independent third party valuation. The resulting gain of $88 million, net of tax and costs was credited directly to retained earnings. The operating results of HIDC for the period January 1, 2000 to November 28, 2000 are included in the consolidated operating results of the Bank for the year ended December 31, 2000.

Following this transaction, HIDC was transferred by the Parent to Merrill Lynch HSBC Limited, a company in which the Group has a 50% interest. Subsequently HIDC was re-named Merrill Lynch HSBC Canada Inc. ("MLHSBC Canada"). The Bank continues to provide a variety of administrative services to MLHSBC Canada on an arm's length basis at market terms and conditions.

The Bank pays fees to Group companies with respect to guarantees of deposit liabilities, administrative and technical services provided to the Bank. The total fees for the year ended December 31, 2001 amounted to $67 million (2000 - $53 million).

Group companies hold certain debentures and preferred shares of the Bank (notes 9 and 10).

The Bank has an agreement with a Group company to provide a standby borrowing facility of up to US$300 million to the Bank at market rates and conditions. Funds have not been drawn from the facility since entering into the agreement.

In addition to the above related party transactions, the Bank has transactions of a routine nature with Group companies, none of which are material to these financial statements.

The Bank's wholly owned principal operating subsidiaries are as follows:

Principal subsidiaries	*Principal office address*		*Book value of voting shares*
HSBC Mortgage Corporation (Canada)	Vancouver, British Columbia	$	227
HSBC Trust Company (Canada)	Edmonton, Alberta		–
HSBC Canadian Direct Insurance Incorporated	New Westminster, British Columbia		35
HSBC Securities (Canada) Inc.	Toronto, Ontario		236
HSBC Capital (Canada) Inc.	Vancouver, British Columbia		8
HSBC Investment Funds (Canada) Inc.	Vancouver, British Columbia		1
HSBC Asset Management (Canada) Limited	Vancouver, British Columbia		5
HSBC Loan Corporation (Canada)	Vancouver, British Columbia		1

HSBC International Network (at 4 March 2002)

Services are provided by some 7,000 offices in 81 countries and territories:

Europe	*Offices*
Armenia	2
Azerbaijan	1
Belgium	4
Channel Islands	25
Cyprus	159
Czech Republic	1
France	790
Germany	12
Greece	57
Ireland	6
Isle of Man	4
Italy	13
Luxembourg	7
Malta	61
Monaco	2
Netherlands	1
Poland	2
Russia	3
Spain	7
Sweden	2
Switzerland	17
Turkey	166
United Kingdom	1,765

Asia-Pacific	*Offices*
Australia	44
Bangladesh	4
Brunei Darussalam	14
China	22
Hong Kong Special Administrative Region	427
India	37
Indonesia	15
Japan	6
Kazakhstan	1
Korea, Republic of	10
Macau Special Administrative Region	6
Malaysia	42
Maldives	1
New Zealand	7
Pakistan	2
Philippines	22
Singapore	27
Sri Lanka	10
Taiwan	20
Thailand	2
Vietnam	2

Americas	*Offices*
Argentina	226
Bahamas	10
Bermuda	2
Brazil	1,632
British Virgin Islands	1
Canada	165
Cayman Islands	4
Chile	2
Guam	1
Mexico	3
Panama	16
Saipan	1
United States of America	946
Uruguay	4
Venezuela	1

Middle East and Africa	*Offices*
Algeria	1
Angola	2
Bahrain	4
Côte d'Ivoire	1
Egypt	14
Ghana	1
Iran	1
Israel	3
Jordan	3
Lebanon	7
Libya	1
Mauritius	13
Morocco	1
Mozambique	2
Namibia	1
Oman	7
Palestinian Autonomous Area	1
Qatar	3
Saudi Arabia	80
South Africa	12
Uganda	2
United Arab Emirates	16

Associated companies are included in the network of offices.

HSBC Bank Canada Branches and Subsidiaries

British Columbia
Abbotsford
Burnaby (3)
Campbell River
Chilliwack
Coquitlam (2)
Cranbrook
Kamloops
Kelowna (2)
Langley
Maple Ridge
Nanaimo (2)
New Westminster
North Vancouver (2)
Penticton
Port Coquitlam
Prince George
Richmond (4)
Surrey (2)
Vancouver (16)
Vernon
Victoria (3)
West Vancouver
White Rock

Alberta
Calgary (5)
Edmonton (4)
Lethbridge
Medicine Hat
Red Deer

Saskatchewan
Regina
Saskatoon

Manitoba
Winnipeg

Ontario
Barrie
Brampton
Etobicoke
Hamilton
Kingston
Kitchener
London
Markham (3)
Mississauga (3)
Oakville
Ottawa
Richmond Hill
St. Catharines
Sault Ste. Marie
Scarborough (3)
Thunder Bay
Timmins
Toronto (8)
Unionville
Vaughan
Whitby
Willowdale
Windsor

Québec
Brossard
Chicoutimi
Laval
Longueuil
Montréal (4)
Pointe-Claire
Québec City
Saint Léonard
Sherbrooke
Trois-Rivières

New Brunswick
Fredericton
Saint John

Nova Scotia
Halifax

Newfoundland
St. John's

United States
Portland
Seattle

SUBSIDIARIES

HSBC Canadian Direct Insurance Incorporated
1 (888) 225-5234
www.canadiandirect.com

HSBC Trust Company (Canada)
1 (888) 887-3388

HSBC Asset Management (Canada) Limited
1 (888) 390-3333
www.hsbc.ca/assetmanagement

HSBC Capital (Canada) Inc.
(604) 631-8088
(416) 369-4748

HSBC Investment Funds (Canada) Inc.
1 (800) 830-8888
www.hsbc.ca/funds

HSBC Securities (Canada) Inc.
1 (800) 332-1182

AFFILIATED COMPANY

Merrill Lynch HSBC Canada Inc.
www.mlhsbc.ca

For more information, or to find the HSBC Bank Canada branch nearest you, call 1 (800) 889-4522 or visit our web site: www.hsbc.ca

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